

# **EU Antitrust Review of Refusal to License IPR: Its Potential for China**

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## LIST OF ABBREVIATIONS

ABA	American Bar Association
AML	Anti-Monopoly Law of the People's Republic of China
CFIUS	the Committee on Foreign Investment in the United States
CJEU	the Court of Justice of the European Union
CNNIC	China Internet Network Information Centre
EEA	the European Economic Area
ETSI	the European Telecommunications Standards Institute
EU	European Union
FRAND	Fair, Reasonable and Non-Discriminatory
GPRS	General Packet Radio Service
ICN	the International Competition Network
IEEE	Institute of Electrical and Electronics Engineers
IM	Instant Messaging
IPR	Intellectual Property Right
IRR	Internal Rate of Return
IT	Information Technology
MOFCOM	the Ministry of Commerce of the People's Republic of China
NDRC	the National Development and Reform Commission of the People's Republic of China
NPV	Net Present Value
OECD	the Organization of Economic Cooperation and Development
R&D	Research and Development
RAND	Reasonable and Non-Discriminatory
SAIC	the State Administration for Industry and Commerce of the People's Republic of China
SEP	Standard Essential Patent
SNS	Social Network Site
SOE	State-Owned Enterprise
SSNIP	Small but Significant and Non-transitory Increase in Price
SSO	Standard Setting Organization
TFEU	Treaty on the Functioning of the European Union

UNCTAD

the United Nations Conference on Trade and Development

US

the United States

WTO

the World Trade Organization

## SUMMARY

Competition law and intellectual property protection are complementary components of a modern industrial policy aimed at fostering innovation and promoting consumer welfare. However, in pursuing these goals, it might be quite difficult in some cases to strike a proper balance between unilateral exercise of intellectual property rights (for instance, unilateral refusal to license by a right owner) and enforcement of competition rules. The right to refuse to license entitles the right owners to prevent their intellectual property from being accessed and copied by other market participants, either competitors or non-competitors. While this can be perfectly legitimate conduct, the effect of such a refusal on the relevant market could be anti-competitive under certain special circumstances. It is a delicate question particularly against the fact that the EU and the US take, to some extent, opposite positions. This difficulty is further enhanced in China by the fact that the newly emerging competition law jurisdiction apparently has not, through its competition law enforcement activities, accumulated sufficient experience in merely six years. Moreover, in the absence of an analytical framework tailored for specific practices of intellectual property right owners, one may raise the concern that industrial policy considerations would be given a superior position by the competition law authorities and prevail over competition policy considerations in individual cases. Thus, it might be safe to conclude that it is necessary for Chinese lawmakers to learn successful international experience in order to examine whether specific unilateral exercise of intellectual property rights by right owners, such as the behaviour of refusal to license, is abusive or not. Thus, the crucial question in this research has become whether, and to what extent, the EU model on refusal to license IPR (and follow-on pricing issue) could be, or has already been transplanted to the Chinese legal and economic context.

The analysis in chapter 1 demonstrates that the major components of the Chinese competition rules are modelled after EU competition law rather than the US antitrust rules. The multiple objectives pursued have been observed to be similar to those in the EU. It is the EU competition law that has influenced most aspects of the three competition law realms of anticompetitive agreements, abuse of dominance and merger review. Apart from the substantial provisions, the enforcement regime of Chinese competition law was found to be also influenced by the EU administrative agency-oriented model. Given the backdrop of the increasingly close EU-China relationship with respect to competition law, it is highly likely that the EU successful experience, *inter alia* in certain complicated competition issues such as those at the intersection of competition law and IPR, could provide further guidance for China.

Chapter 2 and 3 turn to the analysis of the EU approach on refusal to license, and more particularly to the development and definition of the ‘exceptional circumstances test’. Faced with the fundamental question of how the competition rules should be set towards right owners’ unilateral refusal to license behaviour, the CJEU developed the ‘exceptional circumstances test’ to deal with this matter. The CJEU in *Magill* established the main principle in refusal to license IPR cases that the exercise of an exclusive right by the proprietor may, in exceptional circumstances, involve abusive conduct. The EU Commission and Courts however have been at pains in the following cases, including *IMS Health* and *Microsoft*, to interpret the content of the ‘exceptional circumstances test’, namely the three prongs of exceptional circumstances and one prong of justification, in order to improve the legal certainty of the analytical framework for the competition authorities and courts at Member States’ level and the competition law practitioners. After having adopted lower criteria of the ‘exceptional circumstances test’, the EU Commission (and the General Court as well) has demonstrated its interventionist stance towards the refusal behaviour by an undertaking with a dominant position in a market characterized by strong network effects. This stance is even more obvious when compared to the US antitrust authorities’ generally lenient approach on unconditional, unilateral refusal to license.

On top of the substantial criteria established from the perspective of competition towards unilateral refusal to license behaviour, chapter 4 examines royalty setting issue, which as a follow-on matter, could also be related to refusal to license. The analysis distinguishes two situations where the concept FRAND could be related to IPR holder’s refusal to license in non-SEP cases and SEP cases. The EU Commission in *Motorola* FRAND case found that the standardization context and Motorola’s FRAND commitment constitute ‘exceptional circumstances’, thus distinguishing this case from other cases where the general principle that a patent holder has the right to refuse to license could apply. Nevertheless, at the EU level the fact remains that neither the EU Commission nor the EU courts have formulated a predictable approach that allows the IPR holders to evaluate whether their royalty rates comply with the FRAND requirement.

While the EU Commission and EU courts have taken their roles in formulating the EU criteria, the thesis investigates in chapter 5 whether the EU approach could be transplanted, or is being considered by Chinese lawmakers. The case study of *Qihoo/Tencent* has shed some light particularly on the definition of relevant product and geographic market in software industry against the scant judicial experience since the enactment of the AML in China. While the only

IP-related provision within the AML (Article 55) leaves the question unanswered as to whether and under what conditions right owners' refusal to license behaviour would be treated as abuse of dominant position, chapter 5 examines in details the envisaged substantial criteria on refusal to license within the draft *AML IP Guideline* and the draft *IP Enforcement Regulation*. It could be observed that the Chinese lawmakers have in the latest draft of *IP Enforcement Regulation* adopted a *lower* standard to establish an abusive refusal to license. On the one hand, the substantial criteria proposed in the draft *AML IP Guideline* appears closer to the EU approach compared to the much broader essential facility provision provided in the draft *IP Enforcement Regulation*. On the other hand, both of the draft *AML IP Guideline* and the draft *IP Enforcement Regulation* are divergent, to varying degrees, with EU's 'exceptional circumstances test' in many respects. This thesis thus proposes firstly that the *IP Enforcement Regulation* should set the tone for the *AML IP Guideline* owing to their different roles in the competition law system. As to the substantial criteria within the *IP Enforcement Regulation* on refusal to license, this thesis recommends revising Article 7 to contain two parts: a general principle and the exceptional circumstances to establish abusive refusals. It is vital to revise current essential facility provision in the draft *IP Enforcement Regulation* into the EU-like exceptional circumstances. It should be noted that there have been two standards in the EU case law. Considering that it is unlikely that the *IP Enforcement Regulation* would completely copy the strict criteria set out in *IMS Health*, it may be realistic to re-set the Chinese version of competition criteria on refusal to license in between the EU *Magill/IMS Health* standard and the *Microsoft I* standard. As to the potential *AML IP Guideline*, based on the criteria set out in the *IP Enforcement Regulation*, more detailed guidance on assessing refusal to license conduct could be provided after obtaining experience from enforcement authority's future activities. Chapter 5 also reviews the excessive pricing and FRAND-related provisions within the legal instruments and practice in China, *inter alia* the recent *Huawei/IDC* case, demonstrating that in this respect China generally takes an EU-like position. A final remark in this thesis relates to the institutional reform in China, with the aim of overcoming the problems within the current enforcement regime (including inter-authority and intra-authority problems). After finding that merging the three competition law enforcement authorities into one single, independent EU Commission-like enforcement authority is not feasible in the foreseeable future, this thesis proposes to pursue the second best – merging the two competition law divisions under the NDRC and the SAIC into one agency in charge of non-merger cases.



# INTRODUCTION

## 1. General introduction

Although intellectual property laws grant right owners temporary exclusive rights, it has been commonly accepted, by the major competition law authorities, that intellectual property laws and competition law are complementary components of a modern industrial policy aimed at fostering innovation and promoting consumer welfare.<sup>1</sup> Yet, in pursuing these goals it appears quite difficult to make a sound balance between these two instruments. This is complicated further by the fact that both intellectual property rights ('IPRs') and competition law could be closely related to economic theory.<sup>2</sup> It is against this general background that striking the optimal balance between fair market competition and the protection of IPRs has long been the subject of much legal debate.<sup>3</sup> While the convergence has been reached by the European

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<sup>1</sup> For the EU see, *inter alia*, EU Commission, *Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements*, 28 March 2014, OJ C 89/03, Para 7, "Intellectual property rights promote dynamic competition by encouraging undertakings to invest in developing new or improved products and processes. So does competition by putting pressure on undertakings to innovate. Therefore, both intellectual property rights and competition are necessary to promote innovation and ensure a competitive exploitation thereof". For the US see, Department of Justice and Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property*, 6 April 1995, § 1.0, "The intellectual property laws and the antitrust law share the common purpose of promoting innovation and enhancing consumer welfare"; US Department of Justice and Federal Trade Commission in the introduction of the *Antitrust Enforcement & IPRs: Promoting Innovation and Competition* (2007) reiterate that "antitrust enforcers and the courts have to recognize that intellectual property laws and antitrust laws share the same fundamental goals of enhancing consumer welfare and promoting innovation."

<sup>2</sup> Economic analysis in the field of intellectual property rights see, for instance, Edmund W. Kitch, 'Graham v. John Deere Co.: New Standards for Patents' (1966) *Supreme Court Review* 293; William M. Landes and Richard A. Posner, 'Trademark Law: An Economic Perspective', (1987) 30 *Journal of Law and Economics* 265; William M. Landes and Richard A. Posner, 'An Economic Analysis of Copyright Law' (1989) 18(2) *Journal of Legal Studies* 325; Keith E. Maskus, 'Intellectual Property Challenges for Developing Countries: An Economic Perspective' (2001) 2001(1) 457; Joseph E. Stiglitz, 'Economic Foundations of Intellectual Property Rights' (2008) 57(6) *Duke Law Journal* 1693; Drew Voth, Brian Park and Nathan C. Brunette, 'Apportionment of Intellectual Property Value – Where Economic Theory Meets Legal Practice' (2013) 60 (9) *The Federal Lawyer* 72. Economic analysis in the field of competition law, in particular on abuse of dominance, see, for instance, Robert O'Donoghue and A. Jorge Padilla, *The Law and Economics of Article 102 TFEU* (second edition, Hart Publishing 2013); Pinar Akman, *The Concept of Abuse in EU Competition Law: Law and Economic Approaches* (Hart Publishing 2012); Doris Hildebrand, *The Role of Economic Analysis in the EC Competition Rules* (third edition, Wolters Kluwer 2009).

<sup>3</sup> See e.g. Joseph Schumpeter, *Capitalism, Socialism and Democracy* (George Allen & Unwin, 1976); Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996); David J.

Union ('EU') and the United States ('US') in many IPR-related respects, the two competition law jurisdictions have adopted, to varying degrees, different positions in some IPR-related competition law issues.

The right owners' behaviour of refusal to license their rights to other requesting parties is one such example on which the EU and the US have divergent views. The right to refuse to license entitles the right owners to prevent their intellectual property from being accessed and copied by other market participants, either competitors or non-competitors. While this can be perfectly legitimate conduct, the effect of such a refusal on the relevant market could be anti-competitive under certain special circumstances. Contrary to the US antitrust enforcement authorities' view that "[a]ntitrust liability for mere unilateral, unconditional refusals to license patents will not play a meaningful part in the interface between patent rights and antitrust protections"<sup>4</sup>, the European Commission and the EU Courts have shown greater willingness to intervene rather than leave it to the market to correct itself.<sup>5</sup> Whereas the competence of the Court of Justice of the European Union ('CJEU') to deal with substantive matters of intellectual property rights has not been fully acknowledged<sup>6</sup>, it has been firmly established that intellectual property rights are subject to EU competition rules. In those abuse of dominance cases, not only should the possession of a dominant position by an intellectual property owner be proved, but a further requirement, as held by the CJEU in the *Hoffman-La Roche*,<sup>7</sup> that the undertaking at issue has abused such dominant position should also be

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Berber, *Law and Competition in Twentieth Century Europe: Protecting Prometheus* (Clarendon Press 1998); Valentine Korah, *Intellectual Property Rights and the EC Competition Rules* (Hart Publishing 2006); Claus-Dieter Ehlermann and Isabela Atanasiu (eds.), *European Competition Law Annual 2005: The Interaction between Competition Law and Intellectual Property Law* (Hart Publishing 2007); Inge Govaere and Hanns Ullrich (eds.) *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang 2008); Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights: The Regulation of Innovation* (second edition, Oxford University Press 2011); Robert Merkin, 'The Interface between Anti-trust and intellectual Property' (1985) *European Competition Law Review* 377; James Langenfeld, 'Intellectual Property and Antitrust: Steps towards Striking a Balance' (2001) 52(1) *Case Western Reserve Law Review* 91. Striking a optimal balance between competition and intellectual property rights has also been a subject in China, see, *inter alia*, Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed.), *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012), pp.236-242.

<sup>4</sup> U.S. Department of Justice and Federal Trade Commission, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (2007), p6.

<sup>5</sup> See generally R. Hewitt Pate, 'Competition and Intellectual Property in the US: Licensing Freedom and the Limits of Antitrust' in Claus-Dieter Ehlermann and Isabela Atanasiu (eds.), *European Competition Law Annual 2005 : the Interaction between Competition Law and Intellectual Property Law* (Hart Publishing 2007) 49.

<sup>6</sup> See Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), p3.

<sup>7</sup> Case 102/77 *Hoffman-La Roche* [1978] ECR 1139, Para 16.



fulfilled. Thus, the main concern in the EU is where to draw the line to distinguish legitimate refusal to license conduct and abusive refusal behaviour that would raise serious competition policy concerns. The EU courts have established and confirmed in a series of cases the *exceptional circumstances* in which the right owners' conduct of refusal to license IPR might be considered as an infringement of EU competition rules.<sup>8</sup>

As a newly emerging competition law jurisdiction, China in 2007 promulgated its *Anti-Monopoly Law* ('AML') after 13 years of discussions, debates and drafting.<sup>9</sup> In the implementation a number of substantial and procedural rules have been laid down by Chinese competition law enforcement authorities.<sup>10</sup> With regard to the IPR-competition interface, the principle that the protection of IPRs and the enforcement of competition rules are not conflicting has not been contested by the Chinese competition law authorities<sup>11</sup>, nor even by the scholars.<sup>12</sup> The AML provides that the law "does not govern the conduct of business

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<sup>8</sup> See chapter 2 and 3.

<sup>9</sup> *Anti-monopoly Law of the People's Republic of China* (Adopted at the 29th meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China on 30 August 2007 and effective since 1 August 2008). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=6351&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%C2%A2%B6%CF%B7%A8>, last visited on 29 January 2014). After the adoption of the *Anti-Unfair Competition Law of the People's Republic of China* (Adopted by the Third Session of the Standing Committee of the Eighth National People's Congress on 2 September 1993, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=648&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%B2%BB%D5%FD%B5%B1%BE%BA%D5%F9%B7%A8>, last visited on 20 December 2013, hereinafter 'AUCL'), the drafting of the AML was listed in the legislative plan of the Eighth National People's Congress in 1994. For detailed drafting process of China's Anti-Monopoly Law, see H. Stephen Harris, 'Overview of the Context and History of the Drafting of China's Anti-Monopoly Law', ABA Section of Antitrust Law Spring Meeting, 20 April 2007, Washington, D.C., available at <http://apps.americanbar.org/antitrust/at-committees/at-ic/pdf/spring/07/04-20-07-full.pdf>, last visited on 20 December 2013, pp.2-11. For general introduction of the AML see, for example, Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133; Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249.

<sup>10</sup> See chapter 1, section 3.1.

<sup>11</sup> To implement the AML, the State of Administration for Industry & Commerce ('SAIC') has drafted the *Implementing Rules on the Prohibition of Abuses of Intellectual Property Rights for Purposes of Eliminating or Restricting Competition* ('IP Enforcement Regulation') and published the draft for comment on 10 June 2014, available at [http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610\\_145803.html](http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610_145803.html), last visited on 20 July 2014, see more analysis on this draft IP Enforcement Regulation in chapter 5, section 4.2. Article 2 of the draft IP Enforcement Regulation provides that IP laws and competition law share the same fundamental goals of "promoting innovation and efficiency, and enhancing consumer welfare and public interests".

<sup>12</sup> Most Chinese scholars also agree that competition law and intellectual property rights are generally complementary rather than conflicting, see, for instance, Xiaoye Wang, *Anti-Monopoly Law* (Law Press, China

operators to exercise their intellectual property rights under laws and relevant administrative regulations on intellectual property rights”, but shall apply to “business operators’ conduct to eliminate or restrict market competition by abusing their intellectual property rights”.<sup>13</sup> However, this vague provision does not provide any meaningful guidance for assessing specific practices conducted by IPR owners. Although the AML sets out the conditions for refusal to supply, it remains unclear whether or not the prohibition on abusive refusal to supply could be extended to right owners’ unilateral behaviour of refusal to license IPR. Thus, the answer to the question of whether – and if affirmative, under what situations – right owners’ refusal to license IPR would raise competition concerns has not been clarified within the AML.

The phenomenon of legal transplants – “the moving of a rule or system of law from one country to another, or from one people to another”<sup>14</sup> – is commonly observed since it is submitted that “at most times, in most places, borrowing from a different jurisdiction has been the principle way in which law has developed”<sup>15</sup>. It is held that “legal rules are not peculiarly devised for the particular society in which they now operate”<sup>16</sup>. Competition law is “one of the best examples of legal transplants and convergence”.<sup>17</sup> From the perspective of exportation of the EU competition law, the EU’s efforts of internationalization of its competition law have been observed at both multilateral and bilateral levels. At the multilateral level, the EU Commission has been actively involved in the competition law development of several main international forums, including the European Economic Area (‘EEA’), the International Competition Network (‘ICN’), the Organisation of Economic Cooperation and Development (‘OECD’), the United Nations Conference on Trade and Development (‘UNCTAD’) and the World Trade Organisation (‘WTO’).<sup>18</sup> At the bilateral

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2011), pp.160-162.

<sup>13</sup> AML, *supra* note 9, Art. 55.

<sup>14</sup> Alan Watson, *Legal Transplants: An Approach to Comparative Law* (second edition, University of Georgia Press 1993), p21.

<sup>15</sup> Alan Watson, *Society and Legal Change* (second edition, Temple University Press 2001), p98.

<sup>16</sup> Alan Watson, *Legal Transplants: An Approach to Comparative Law* (second edition, University of Georgia Press 1993), p96.

<sup>17</sup> John O. Haley, *Antitrust in Germany and Japan: The First Fifty Years, 1947-1998* (University of Washington Press 2001), p172.

<sup>18</sup> See Qianlan Wu, ‘EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law?’ (2012) 18(3) *European Law Journal* 461, p464. More analysis of the internationalization of EU competition law at the multilateral level could generally see Anestis Papadopoulos, *The International Dimension of EU Competition Law and Policy* (Cambridge University Press 2010), and more information about this issue could see the official website of the EU Commission at <http://ec.europa.eu/competition/international/multilateral/>, last visited

level, the EU Commission has established cooperation with competition authorities of many jurisdictions outside of the EU, through signing dedicated agreements, or signing general agreements containing competition provisions with other competition law jurisdictions.<sup>19</sup> During the 1990s, the EU and the US competed in central and eastern European countries, Japan and Latin America countries to advocate their competition law models.<sup>20</sup> It is thus interesting in this respect to examine whether the EU is competing with the US to export its own competition law model into China. By fostering a EU-like competition law model in China, the EU could also be benefited on the grounds that, for one thing the influence of the EU model in the global competition law development would be significantly increased, and for another the obstacles relating to competition law issues in future EU-China trade negotiations could, to a great extent, be removed by such bilateral cooperation.<sup>21</sup> From the perspective of China's policy-makers, EU's willingness to intervene in refusal to license cases could be one reason for the hypothesis that China is highly likely to transplant the EU's experience to its own mode of market governance, as the Chinese government is normally perceived as reluctant to leave the market to correct the market failure itself. In recent years, China has become more active in absorbing international legal norms and successful experience on market development into its own legal system.<sup>22</sup> The AML in many aspects follows EU practices and adopts a similar scheme of abuse of dominant position.<sup>23</sup> While the IPR-competition intersection is a relatively new issue in China in general, for a new competition law jurisdiction with merely six years' enforcement experience, how to treat right owners' conduct of refusal to license is a, even more, delicate question particularly against the fact that the EU and the US take, to some extent, opposite positions. Thus, the crucial question in this research has become whether, and to what extent, the EU model on refusal to license IPR could be transplanted to the Chinese legal and economic context. The following section gives an overview of the research questions raised in each chapter of the thesis.

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on 9 April 2014.

<sup>19</sup> <http://ec.europa.eu/competition/international/bilateral/>, last visited on 9 April 2014.

<sup>20</sup> See e.g. Eleanor M. Fox, 'The Central European Nations and the EU Waiting Room – Why Must the Central European Nations Adopt the Competition Law of the European Union?', (1997) 23 *Brooklyn Journal of International Law* 351; Spencer Weber Waller, 'Neo-Realism and the International Harmonization of Law: Lessons from Antitrust', (1994) 42 *University of Kansas Law Review* 557; Malcolm B. Coate, Rene Bustamante and A.E. Rodriguez, 'Antitrust in Latin America: Regulating Government and Business', (1992) 24 *University of Miami Inter-American Law Review* 37.

<sup>21</sup> See Qianlan Wu, 'EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law' (2012) 18(3) *European Law Journal* 461, p475.

<sup>22</sup> See generally Pitman B. Potter, 'Globalization and Economic Regulation in China: Selective Adaptation of Globalized Norms and Practices' (2003) 2 *Washington University Global Studies Law Review* 119.

<sup>23</sup> See chapter 1.

## 2. Research questions, scope and structure of the research

Beside this introduction and the final conclusion, the substantial part of this thesis consists of five chapters. The main research question put forward above will be answered in two steps. First, it will examine the current approach adopted by the EU Commission and the EU courts on a dominant IP holder's unilateral conduct of refusal to license as well as their position on the follow-on pricing issue. Second, whether and to what extent the EU model could contribute to China's anti-monopoly practice with respect to this specific issue will then be addressed. However, prior to the two-step analysis, a crucial question that should be addressed at the outset is, compared to the US antitrust law, whether the current Chinese competition law in many respects resembles the EU competition rules. In other words, the link connecting the EU and China in terms of their competition law systems will be firstly established in chapter 1. It will be possible to make a preliminary conclusion that China is more willing to import the EU approach on refusal to license IPR only if the answer to this pre-question is affirmative. To establish such a link, chapter 1 will analyze from two different angles. Given the background of the growing economic and trade ties between the EU and China, chapter 1 will investigate the similarities between the current Chinese competition system and the EU competition law regime. First, whether the EU competition law and Chinese anti-monopoly law similarly pursue multiple objectives? Second, whether the enforcement regime of Chinese anti-monopoly law is EU-like? Third, with regard to specific rules, whether the substantial provisions in the three competition law pillars – anticompetitive agreements, abuse of dominance and merger in Chinese anti-monopoly law (and in other implementing regulations) are akin to the EU competition rules? The answers could, to some extent, demonstrate whether Chinese lawmakers have in general perceived EU competition law, compared to the US antitrust law, as a more suitable model for China to follow. In addition, chapter 1 will investigate the unsolved issues within the current Chinese competition law legislations, and the inter-authority and intra-authority problems existing within the administrative enforcement regime and the judicial system, aiming to analyze whether China is still urgently in need of further guidance from the EU experience, *inter alia* in certain complicated competition issues such as refusal to license IPR.

In order to merge foreign legal elements into a new system, it is fundamental to “re-contextualize them by examining how and why they were created, how they have developed”.<sup>24</sup> Thus, the subsequent chapter 2 and chapter 3 provide a thorough analysis of the

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<sup>24</sup> David J. Gerber, ‘Constructing Competition Law in China: The Potential Value of European and U.S. Experience’ (2004) 3 *Washington University Global Studies Law Review* 315, p316.

analytical framework in the EU regarding refusal to license. Upon the introduction of the European Commission's *Guidance on its enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings* ('Commission Guidance')<sup>25</sup>, the EU has shifted towards a more economic based approach. Since Article 102 TFEU does not offer guidance on how the competition rules would be applied in IPR-related cases, it is important in this respect to heavily rely on the case law of the CJEU. In the EU it is apparently recognized by the laws of the Member States that an undertaking, even holding a dominant position on a relevant market, in most cases is free to decide its business strategy and to choose its trading partner.<sup>26</sup> With respect to IPR licensing, the EU courts have in a number of cases confirmed that it is at the discretion of the right holder to license, or otherwise to refuse to license, its IPR to a third party, including its competitors.<sup>27</sup> Only under some recognized exceptional circumstances, which have been developed by the EU courts in significant cases such as *Magill*<sup>28</sup>, *IMS Health*<sup>29</sup> and *Microsoft*<sup>30</sup>, shall the dominant undertakings be ordered to license their IPRs to new customers or continue their licensing relations with current customers.<sup>31</sup> Otherwise, an abusive refusal to license IPR would lead to limiting competitors' production, or impeding technical development of certain neighbouring market to the prejudice of consumers within the meaning of Article 102 TFEU. Since such 'exceptional circumstances test' has mainly been developed in aforementioned cases, it is necessary to revisit them. Furthermore, a detailed analysis of related EU competition law principles and concepts is necessary in order to understand the EU model as an integrated system. This analysis not only includes the traditional issues such as defining the relevant market and assessing the existence of dominant position. The latter could be quite complicated and controversial in some 'dynamically competitive industries', such as information technology ('IT') industry, where a high market share may not indicate strong market power. The analysis also involves some novel issues and concepts, such as the economic efficiency (dynamic & static efficiency) and

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<sup>25</sup> Communication from the Commission – *Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings*, [2009] OJ C45/7.

<sup>26</sup> Judgment in *Oscar Bronner*, C-7/97, ECLI:EU:C:1998:264, opinion of Mr Advocate General Jacobs delivered on 28 May 1998, Para 53 and 56.

<sup>27</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, Para 7-8; Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para. 49; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para. 34 Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 331.

<sup>28</sup> Judgment in *Magill* ECLI:EU:C:1995:98, *supra* note 27.

<sup>29</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 27.

<sup>30</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, *supra* note 27.

<sup>31</sup> Judgment in *Volvo* ECLI:EU:C:1988:477, *supra* note 27, Para 9; Judgment in *Magill* ECLI:EU:C:1995:98, *supra* note 27, Para 50; Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 27, Para 35; Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, *supra* note 27, Para 319, 330, 331, 332 and 336.

commitment decision.

Thus, chapter 2 will address following research questions: (1) how the consumer welfare and economic efficiency, as prominent EU competition law objectives, perform in refusal to license cases? (2) How the relevant market and dominant position could be determined in IPR-related cases, in particular in those dynamically competitive industries? (3) As to the substantial criteria in assessing whether right owners' refusal to license constitutes an abuse of dominant position, much attention will be paid on the analysis of how such 'exceptional circumstances' has been established and interpreted by the CJEU (except the General Court's *Microsoft I* judgment), what elements they are composed of and which criteria can be used to identify them. (4) Which type of decision (Article 7 or Article 9 of Regulation 1/2003<sup>32</sup>) and which type of remedy is possible and appropriate in refusal to license cases?

Chapter 3 is dedicated to analyse the EU Commission's decision and the General Court's judgment in the *Microsoft I* refusal to disclose interoperability information case<sup>33</sup> in order to observe the most recent development of the 'exceptional circumstances test'. The main research questions in this case study are as follows: (1) how have the conditions 'indispensability' and 'elimination of competition' been interpreted by the EU Commission and the General Court respectively? Are these two conditions in fact the two sides of a coin? (2) Is the *Microsoft I* case a progress or a retreat in terms of the 'new product condition' broadly interpreted by the General Court? (3) Did the General Court take an explicit position on the 'incentive balance test' proposed by the EU commission in its decision? (4) Compared with US approach on refusal to license, where does the balance lie between consumer and competitor protection in the EU?

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<sup>32</sup> Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Article 81 and 82 of the Treaty, [2003] OJ L1/1.

<sup>33</sup> The European Union *Microsoft* competition case involved in this research includes two judgments of the General Court: Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289 (appealed against COMP/C-3/37.792, Commission Decision of 24 March 2004), and Judgment of 27 June 2012, *Microsoft v Commission*, T-167/08, ECR, ECLI:EU:T:2012:323, (appealed against COMP/C-3/37792, Commission Decision of 27 February 2008). Throughout this research the former interoperability information case will be referred to as '*Microsoft I*', while the Microsoft compliance case, which deals with follow-on pricing issue, will be referred to as '*Microsoft II*' mainly in chapter 4. In some paragraphs of this thesis, it reads as 'the *Microsoft* case' without indicating whether it is *Microsoft I* or *Microsoft II*. In those cases, unless specified otherwise, the *Microsoft* case means the 2004 Commission Decision and the 2007 General Court judgment on interoperability information issue.

There might be two things an IPR holder who refuses to grant other undertakings a license to access to his IPR cares about the most. One is whether his refusal to license constitutes an abuse of dominant position under the competition rules, which is the subject of chapter 2 and 3. The other follow-on pricing-related concern, as the subject of chapter 4, is how much benefits the right owner could reap from licensing his IPR once he is ordered by the competition authority to grant requesting parties a licence. This involves the term *fair, reasonable and non-discriminatory* ('FRAND', or in US 'RAND'), which is an IPR-competition intersection expression. Depending on whether the IP at issue is standard essential patent ('SEP') and whether the IPR holder has committed to standard-setting organizations ('SSOs') that he will license his IPR to third parties on FRAND terms, there might be two situations where the concept FRAND would be involved in one dominant undertaking's conduct of refusal to license IPR. One situation could be the scenario where the SEP holder, who committed in standardization to the SSO to license his SEP on FRAND terms<sup>34</sup>, seeks and enforces an injunction against specific third party before a court on the basis of his SEP. Apart from SEP cases, the concept FRAND also emerges in non-SEP cases, such as *IMS Health* and *Microsoft I and II*, where the conduct of refusal to license IPR has, in exceptional circumstances, been considered abusive under Article 102 TFEU, irrespective of previous relationship between the licensor and the licensees. Chapter 4 will connect the royalty setting issue with right owners' dominant position and their previous refusal behaviour. Thus chapter 4 is complementary to the issues dealt with in chapter 2 and 3. From the perspective of protection of innovation incentives, IPR holders should be compensated for their investment on R&D. From the perspective of competition policy, the prices that IPR holders set for access to their IPRs should not be unfairly high, since excessive pricing might trigger the competition authority's investigation into whether such behaviour has again abused the IPR holder's dominant market position. For China it is also a crucial question under what conditions the IPR holders should license their IPRs, or specifically at what level the IPR holders should set the royalties once the conduct of refusal to license has been found unlawful. Chapter 4, firstly from a legal perspective, will investigate EU's FRAND concept. Secondly, this chapter will, from an economic perspective, introduce some economic approaches to determining a FRAND royalty rate and then analyse their applicability in follow-on refusal to license cases.

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<sup>34</sup> For example, the IPR Policy of the European Telecommunications Standards Institute ('ETSI') provides that when an IPR holder discloses his essential IPR to the ETSI, the holder would be requested to give "an irrevocable undertaking in writing that it is prepared to grant irrevocable licences on fair, reasonable and non-discriminatory ('FRAND') terms and conditions" to those who seek such license and thus waive its right to refuse to grant a license. See ETSI IPR Policy, section 6.1, available at <http://www.etsi.org/images/files/IPR/etsi-ipr-policy.pdf>, last visited on 18 November 2013.

Chapter 5 will explore and elaborate how the EU approaches in terms of refusal to license and the follow-on pricing issue should be transplanted – in entirety or in part – to the Chinese legal and economic context. The main questions to be answered in this chapter are, firstly whether the EU approaches on refusal to license IPR and the follow-on pricing issue are being considered by the Chinese lawmakers as the primary reference in Chinese competition legislations, secondly what significant observations could be made in Chinese administrative authorities’ and the courts’ enforcement of the AML in IP-related cases, and thirdly what institutional reform could be reasonably expected. The legal uncertainty of Article 55 of the AML has firstly raised one pre-question as to whether this Article “may have extended the scope of the prohibition on abusing a dominant market position to activities that non-dominant companies carried out in an IP context”.<sup>35</sup> Chapter 5 will analyze, through studying a recent significant civil litigation between two Chinese software companies Qihoo and Tencent and comparing it with EU cases in terms of relevant market definition and dominance assessment, whether the possession of a dominant position is a ‘must have’ precondition in the IP context in the ‘normal’ abuse of dominance cases (as well as the relevant market definition in IPR-intensive industries). As to the substantial criteria on refusal to license, the ambiguity of Article 55 of the AML leaves a number of questions unanswered, including, *inter alia*, (1) whether an unconditional and unilateral refusal to license would constitute an abuse of dominant position? (2) What obligation competition authority would impose on the IPR holder once his refusal to license is found to violate anti-monopoly rules, and (3) whether refusal to license IPR would be equally treated as refusal to conclude other contracts? This chapter will examine relevant provisions – including envisaged general provisions and specific articles on refusal to license issue – within two legal documents in draft, the *Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights* (‘AML IP Guideline’)<sup>36</sup> and the *Implementing Rules on the Prohibition of Abuses of Intellectual Property Rights for Purposes*

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<sup>35</sup> Yijun Tian, ‘The Impacts of the Chinese Anti-Monopoly law on IP Commercialization in China & General Strategies for Technology-driven Companies and Future Regulators’, (2010) 4 *Duke Law & Technology Review* 1, p10.

<sup>36</sup> The fifth draft AML IP Guideline was released in the International Symposium of Forefront Issues of Anti-Monopoly Law Enforcement on 14 August 2012. An unofficial English translation is available as an appendix to the Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights, available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014.



*of Eliminating or Restricting Competition* ('IP Enforcement Regulation')<sup>37</sup>. By analyzing these provisions – still in the drafting progress though, it aims to explore whether potential Chinese criteria on refusal to license will resemble EU's 'exceptional circumstances test', or it will take a position like the US where "[a]ntitrust liability for mere unilateral, unconditional refusals to license patents will not play a meaningful part in the interface between patent rights and antitrust protections"<sup>38</sup>. This chapter will also investigate the follow-on pricing issue (following an abusive refusal to license finding), by analyzing the FRAND-related provisions within Chinese competition legislations and significant royalty rate setting cases in practice. On top of aforementioned substantial issues related to refusal to license, this chapter will seek whether it is necessary, and if affirmative, how to make institutional reforms within current AML enforcement regime to suit China's unique needs with respect to competition-IP interface in general and the refusal to license issue in particular.

### 3. Methodology

The research involves an analysis of the EU approach on refusal to license intellectual property rights, concentrating on the so-called 'exceptional circumstances test'. Since such approach is established by EU courts to examine whether the refusal to license behaviour is abusive, case law analysis is of major importance in this research. Relevant EU cases are revisited mainly in chapter 2 and 3, complemented with an analysis of some relevant competition law concepts, in particular the existence of a dominant position in dynamically competitive industries which issue will be again touched upon in a significant Chinese competition law case in chapter 5. Once it is clarified how the EU model distinguishes an abusive refusal to license and a legitimate refusal to license, chapter 4 aims to answer a follow-on question as of how should the right owners, after an abusive refusal to license has been found, set the licensing fees to fulfil the FRAND requirement and avoid excessive pricing, where some economic models are involved. With regard to the potential approach on refusal to license in China, the research mainly relies on the analysis of its national legislative provisions, whether in force or still in drafting progress, since except the on-going investigation against Microsoft's alleged refusal to disclose interoperability information in China<sup>39</sup> there is no settled refusal to license case before either the courts or Chinese competition law authorities.

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<sup>37</sup> See *supra* note 11.

<sup>38</sup> See *supra* note 4.

<sup>39</sup> See chapter 5, section 4.1.

In addition to extensive literature studies and case law analysis, the research also incorporates comparative analysis. To examine whether and to what extent the EU model on refusal to license could be transposed to China, a comparison between the competition law objectives in the EU and those in China, as well as other important competition rules in force (other than rule on refusal to license) in three pillars – merger, anti-competitive agreements and abuse of dominance, will be conducted in chapter 1. More importantly, the envisaged China's analytical framework on refusal to license, which is in the drafting progress, is compared to the EU model in chapter 5, aimed at responding to the question of whether the more economic based approach adopted by the EU Commission and EU courts on refusal to license could be applied in China's legal and social environment. Furthermore, this research involves comparative analysis of different models adopted by the EU and the US with respect to the refusal to license issue, as well as follow-on pricing issue, throughout the thesis in order to examine whether the EU approach would fit better for China. The thesis states the law and state of play in the case law as of 20 November 2014.

# CHAPTER I China and EU: the learner and the (potential) tutor?

## 1. Introduction

After 13 years of discussions, debates and drafting, in 2007 China promulgated its *Anti-Monopoly Law* ('AML').<sup>1</sup> As displayed in the table 1 below, the AML is composed of eight chapters and 57 articles. It is noticeable that the AML covers the three pillars of modern competition law – anticompetitive agreements, abuse of dominant position and merger control – in three main chapters (Chapter 2, 3 and 4 of the AML). The AML, as the fundamental competition law, not only lays down competition rules for regulating the activities of economic entities participating in the marketplace in China, but also prevents Chinese administrative bodies from abusing their power to eliminate or restrict competition. (Chapter 5 of the AML)

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<sup>1</sup> *Anti-monopoly Law of the People's Republic of China* (Adopted at the 29th meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China on 30 August 2007 and effective since 1 August 2008). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=6351&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%C2%A2%B6%CF%B7%A8>, last visited on 29 January 2014). After the adoption of the *Anti-Unfair Competition Law of the People's Republic of China* (Adopted by the Third Session of the Standing Committee of the Eighth National People's Congress on 2 September 1993, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=648&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%B2%BB%D5%FD%B5%B1%BE%BA%D5%F9%B7%A8>, last visited on 20 December 2013, hereinafter 'AUCL'), the drafting of the AML was listed in the legislative plan of the Eighth National People's Congress in 1994. For detailed drafting process of China's Anti-Monopoly Law, see H. Stephen Harris, 'Overview of the Context and History of the Drafting of China's Anti-Monopoly Law', ABA Section of Antitrust Law Spring Meeting, 20 April 2007, Washington, D.C., available at <http://apps.americanbar.org/antitrust/at-committees/at-ic/pdf/spring/07/04-20-07-full.pdf>, last visited on 20 December 2013, pp.2-11. For general introduction of the AML see, for example, Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133; Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249.

**Table 1: Scheme of the AML**

<b>Chapter of the AML</b>	<b>Title of Chapter</b>	<b>Articles in Chapter</b>
Chapter 1	General Provisions	Articles 1-12
Chapter 2	Monopoly Agreements	Articles 13-16
Chapter 3	Abuse of Dominant Market Position	Articles 17-19
Chapter 4	Concentration of Business Operators	Articles 20-31
Chapter 5	Abuse of Administrative Power to Eliminate or Restrict Competition	Articles 32-37
Chapter 6	Investigation into Suspicious Monopolistic Conducts	Articles 38-45
Chapter 7	Legal Liabilities	Articles 46-54
Chapter 8	Supplementary Provisions	Articles 55-57

The drafting process of the AML was open domestically and externally, though on a limited basis, and gained valuable comments from individual Chinese and non-Chinese enforcement officials, scholars and practitioners from the foreign jurisdictions such as United States, European Union, Japan, South Korea, and organizations such as OECD, the World Bank, the United Nations Conference on Trade and Development and the Asia-Pacific Economic Cooperation.<sup>2</sup> The adoption of the AML demonstrates that China has made efforts to build its competition mechanism to fit into the global market in the transition from a central-planned economy to a market economy.<sup>3</sup> The economic growth of China – mainly due to the strategic reforms domestically and the process of globalisation externally – would not be sustained nowadays if the standards adopted in its fundamental laws, such as the Anti-Monopoly Law, are inconsistent with the mainstream ideas thereof in the rest of the world.<sup>4</sup>

In order to answer the question of whether and to what extent the pattern adopted by the EU Commission and the EU courts to tackle refusal to license intellectual property rights could

<sup>2</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p237; Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133, p134; Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp. 90-91; Mark S. Blodgett, Richard J. Hunter, Jr. and Robert M. Hayden, 'Foreign Direct Investment, Trade, and China's Competition Laws' 2009 37(2) *Denver Journal of International Law and Policy* 201, p213.

<sup>3</sup> See Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133, pp.133-134.

<sup>4</sup> Eva Choi, 'Seeking Stones in the Red River: The Inevitable Evolution of China's Anti Monopoly Law' (2010) 7(1) *Journal of Law, Economics & Policy* 163, p193.

contribute to China's anti-monopoly practice with respect to this specific issue, the link connecting the EU and China should be firstly established. Despite still existing bilateral disputes on industrial policies, government intervention in the economy, protection of intellectual property rights and so forth, the trade relation between the EU and China has dramatically increased during past decades especially since China's accession to the World Trade Organization in 2001. By far China has become EU's second trading partner behind US, and EU is China's biggest trading partner.<sup>5</sup> Against the background of increasingly close EU-China economic relationship, it is a crucial question and should be addressed at the outset in this research as to whether the EU competition law, compared to competition laws of other jurisdictions (particularly the US), is in such a position that China is more willing to consider EU's successful experience in competition law practice as the target model.

Prior to the adoption of the AML, Professor John Haley argued that neither the EU competition model nor the US antitrust law may be applicable in China.<sup>6</sup> Nevertheless, it appears that the provisions of the AML is in general consistent with the prevailing, internationally accepted practices<sup>7</sup>, while the AML has been criticized, by an US commentator, to keep certain "vestigial" provisions importing from the EU or German (such as accepting presumptions of collective dominance in Article 19, and prohibiting dominant undertakings from selling their products at unfairly high prices in Article 17 of the AML<sup>8</sup>). Although the US entities, such as the American Bar Association,<sup>9</sup> were the most active in commenting

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<sup>5</sup> In 2013 EU-China bilateral trade in goods reached €428.4 billion, and trade in services at €52.8 billion. See <http://ec.europa.eu/trade/policy/countries-and-regions/countries/china/>, last visited on 20 October 2014.

<sup>6</sup> See John O. Haley, 'Competition Policy for East Asia' (2004) 3(2) *Washington University Global Studies Law Review* 277, p277.

<sup>7</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p91.

<sup>8</sup> *ibid*, fn13.

<sup>9</sup> See e.g. Joint Submission of the American Bar Association's Sections of Antitrust Law and International Law and Practice on the Proposed Anti-Monopoly Law of the People's Republic of China (15 July 2003), ('2003 ABA comments'), in supplementation of the Joint Submission of the American Bar Association's Sections of Antitrust Law, Intellectual Property Law and International Law on the Proposed Anti-Monopoly Law of the People Republic of China (19 May 2005), available at [http://www.americanbar.org/content/dam/aba/administrative/antitrust\\_law/comments\\_prc2005wapp.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_prc2005wapp.authcheckdam.pdf), last visited on 20 January 2014; Joint Submission of the American Bar Association's Sections of Antitrust Law, Intellectual Property Law and International Law on the Proposed Anti-Monopoly Law of the People Republic of China (19 May 2005), ('2005 ABA comments') available at [http://www.americanbar.org/content/dam/aba/administrative/antitrust\\_law/comments\\_prc2005wapp.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_prc2005wapp.authcheckdam.pdf), last visited on 20 January 2014; Proposed Revisions to Selected Articles of The April 8, 2005 Revised Draft of The anti-Monopoly Law of the People's Republic of China, In Supplementation of the Joint Submission of the American Bar Association's Sections of Antitrust Law, Intellectual Property Law and International Law, On the

several drafts of the AML, the US antitrust model has not been largely followed by the Chinese lawmakers.<sup>10</sup> Rather, in the early years China began to learn competition theories mainly from German scholars.<sup>11</sup> Both the Chinese and foreign experts have noticed that different versions of AML drafts appear to have been, to varying degrees, influenced by the EU competition law (as well as German competition law).<sup>12</sup>

The most important reason lies in that China found it difficult to follow the US model since China has generally been regarded, to some extent, as having a civil law tradition.<sup>13</sup> Secondly, as will be elaborated in the following section, unlike the US model where economic efficiency is perceived as the exclusive objective of its antitrust law,<sup>14</sup> the EU model is likely to be more instructive to Chinese policymakers since the AML, like EU competition policy, is expected to serve a variety of objectives – even those noncompetition-related policy concerns.<sup>15</sup> The third possible explanation might be the previous adoption of the EU model by most economies in transition.<sup>16</sup> Additionally, another factor contributing to China absorbing experience from the EU on competition policies is the existence of local protectionism, namely Chinese competition authorities and courts in local provinces and cities may be tempted to unduly protect local enterprises in the face of external competition. This is

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Proposed Law, dated 19 May 2005, p27, available at [http://docs.law.gwu.edu/facweb/dclarke/chinalaw/features/documents/ABA\\_July05Comments-PRC\\_AML.pdf](http://docs.law.gwu.edu/facweb/dclarke/chinalaw/features/documents/ABA_July05Comments-PRC_AML.pdf), last visited on 20 January 2014.

<sup>10</sup> See Mark Furse, ‘Competition Law Choice in China’, (2007) 30(2) *World Competition* 323, p325; Eva Choi, ‘Seeking Stones in the Red River: The Inevitable Evolution of China’s Anti Monopoly Law’ (2010) 7(1) *Journal of Law, Economics & Policy* 163, pp.168-170.

<sup>11</sup> See Xiaoye Wang, ‘My Journey on the Anti-Monopoly Law Research’, preface of the forthcoming book by Xiaoye Wang, *The Evolution of China’s Anti-Monopoly Law* (to be published by Edward Elgar), available at <http://www.iolaw.org.cn/showArticle.asp?id=3687> (in Chinese), last visited on 28 November 2013.

<sup>12</sup> See Xiaoye Wang, ‘Highlights of China’s New Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 133, pp.134-135; 2003 ABA comments, *supra note* **Error! Bookmark not defined.**, Executive Summary; 2005 ABA comments, *supra note* **Error! Bookmark not defined.**, fn3.

<sup>13</sup> See Youngjin Jung and Qian Hao, ‘The New Economic Constitution in China: A Third Way for Competition Regime’ (2003) 24(1) *Northwestern Journal of International Law & Business* 107, pp.124-125.

<sup>14</sup> See, for instance, Robert Bork, *The Antitrust Paradox: A Policy at War with Itself* (Basic Books, 1978), p61.

<sup>15</sup> See, for instance, Youngjin Jung and Qian Hao, ‘The New Economic Constitution in China: A Third Way for Competition Regime’ (2003) 24(1) *Northwestern Journal of International Law & Business* 107, pp.123-125; David, J. Gerber, ‘Constructing Competition Law in China: The Potential Value of European and U.S. Experience’ (2004) 3 *Washington University Global Studies Law Review* 315, pp.326-328. See *infra* section 2.1.3 Multiple and (potentially) conflicting objectives.

<sup>16</sup> See Eleanor M. Fox, ‘The Central European Nations and the EU Waiting Room – Why must the Central European Nations Adopt the Competition Law of the European Union?’ (1997) 23 *Brooklyn Journal of International Law* 351.

an area where valuable experience could be provided by the EU who employed various measures in the early years to remove obstacles between Member States in creating a single market.<sup>17</sup> As a consequence, apart from the similar administrative agency-oriented model, the major components of the AML text are modelled after EU competition law.<sup>18</sup> The second section of this chapter will review the objectives, the most important provisions of the AML, and compare them with the EU competition rules, and sometimes with the US antitrust law as well. The third section will analyse in detail the AML enforcement regime, the problems and difficulty in implementing the AML. The fourth section will investigate the institutional cooperation between Chinese enforcement authorities and the EU Commission. This chapter intends to examine whether, firstly, the influence of EU competition law upon the AML text has already been apparent. Secondly, whether the current problems in implementing the AML and the increasingly close EU-China relationship with respect to competition law lead to the conclusion that it is highly likely that the EU successful experience could provide further guidance for China. Thus, this chapter could set the scene for the following chapters.

## **2. The similarities between the AML and EU competition law**

### **2.1 Objectives**

In general, competition law objectives should be set in compliance with, and function as an indicator of, the current values and goals of a society in particular.<sup>19</sup> Compared to other

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<sup>17</sup> See R. Hewitt Pate, 'What I heard in the Great Hall of the People – Realistic Expectations of Chinese Antitrust' (2008) 75 *Antitrust Law Journal* 195, pp.209-210; Mark Furse, 'Competition Law Choice in China', (2007) 30(2) *World Competition* 323, p327.

<sup>18</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.92-93; Yin Zhou, 'China's Anti-Monopoly Law: Insights from U.S. and EU Precedents on Abuse of Dominance and IP Exemption Provisions' (2009) 32(2) *Hastings International and Comparative Law Review* 711, p728; Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p252; Maher M Dabbah, 'The Development of Sound Competition Law and Policy in China: An (Im)possible Dream', (2007) 30(2) *World Competition* 341, p354; Youngjin Jung and Qian Hao, 'The New Economic Constitution in China: A Third Way for Competition Regime' (2003) 24(1) *Northwestern Journal of International Law & Business* 107, pp.124-125; Susan Beth Farmer, 'The Evolution of Chinese Merger Notification Guidelines: A Work in Progress Integrating Global Consensus and Domestic Imperatives' (2009) 18 *Tulane Journal of International and Comparative Law* 1, p6 and 9. Apart from relevant EU competition law and German competition rules, the AML has also been influenced by Japan's Antimonopoly and Maintenance of Fair Trade Act, Taiwan's Fair Trade Act, and South Korea's Monopoly Regulation and Fair Trade Act. See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.92-93.

<sup>19</sup> See Xiaoye Wang and Jessica Su, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar Publishing 2012) 379, p382.

jurisdictions particularly the US, China has quite different social, political, economic, and legal conditions upon which the Chinese competition rules are established.<sup>20</sup> Therefore, prevailing foreign theories and practices must be “re-contextualized” to suit China’s unique conditions.<sup>21</sup>

Since the 1970s, the Chicago School perspective on antitrust argued that the sole purpose of US antitrust law should be to promote economic efficiency for the benefit of consumers.<sup>22</sup> Thus, the US antitrust policy has evolved from a system of multiple objectives which were based on political, social and ideological considerations, to the single goal of economic efficiency.<sup>23</sup> On the other side of the Atlantic, however, a heavy emphasis has also been placed on other objectives, such as market integration and consumer welfare, while economic efficiency has also played an important role in Europe. Although some commentators contend that social and political goals are non competition-related and should not be incorporated into the competition law,<sup>24</sup> the objectives pursued by the AML has been observed to be similar to those in the EU, or the US antitrust policies prior to the Chicago School.<sup>25</sup>

From the perspective of EU Commission, *construction and preservation of the internal market* and *promotion of consumer welfare* have been explicitly recognized as two major objectives through the entire history of EU competition policy.<sup>26</sup> These two objectives have been taken into consideration even since the first EU Commission (‘Community Commission’ at that time) Report on Competition Policy in 1971<sup>27</sup>, though defined differently then<sup>28</sup>. To prevent

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<sup>20</sup> See e.g. Xianchu Zhang, ‘An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy’ (2009) 43*The International Lawyer* 1469, pp.1470 and 1489.

<sup>21</sup> Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p97.

<sup>22</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, pp.58-59. See also Robert H. Bork, *The Antitrust Paradox: A Policy at War with Itself* (Basic Books 1978), p427.

<sup>23</sup> See Robert Bork, *The Antitrust Paradox: A Policy at War with Itself* (Basic Books, 1978), p61; Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, pp.54, 56-59.

<sup>24</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, ‘Antitrust in China: The Problem of Incentive Compatibility’ (2005) 1(1) *Journal of Competition Law and Economics* 123, p142.

<sup>25</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p63.

<sup>26</sup> EU Commission *Annual Report on Competition Policy 2010*, Brussels, 10 Jun 2011, available at [http://ec.europa.eu/competition/publications/annual\\_report/2010/part1\\_en.pdf](http://ec.europa.eu/competition/publications/annual_report/2010/part1_en.pdf), last visited on 29 Feb 2012, Para 1, 9-18.

<sup>27</sup> EU Commission *1<sup>st</sup> Annual Report on Competition Policy 1971*, Brussels – Luxembourg, Apr 1972, available at [http://ec.europa.eu/competition/publications/annual\\_report/ar\\_1971\\_en.pdf](http://ec.europa.eu/competition/publications/annual_report/ar_1971_en.pdf), last visited on 29 Feb 2012, p13 and Part Four “Consumer Protection”.



undertakings from reducing the welfare of the final consumer, as the objective of EU competition law in particular, was confirmed by the General Court respectively in *Österreichische Postsparkasse* case<sup>29</sup> and *GlaxoSmithKline* case<sup>30</sup> in 2006.

However, in literature there is not a commonly accepted view, and it is vague that for what EU competition law is precisely pursuing.<sup>31</sup> For example, Bishop and Walker regard the market integration and the economic goal to be of essential importance;<sup>32</sup> Motta takes into account not only economic efficiency and market integration, but also social and political reasons;<sup>33</sup> Monti identifies three: economic freedom, market integration and efficiency;<sup>34</sup> Fairness, welfare and efficiency, and market integration are three main goals proposed by Ahlborn and Padilla;<sup>35</sup> Anderman and Schmidt consider three distinct objectives in EU competition law: maintenance of effective competition, maintenance of fair competition (protection for small and medium-sized companies) and building up the single market;<sup>36</sup> Paulis takes the protection of consumer welfare for the ultimate goal;<sup>37</sup> Eilmansberger however doubts that efficiency gains

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<sup>28</sup> For example, in EU Commission Annual Report 2010, consumer welfare is defined as “ensuring that markets can deliver the best outcomes for consumers in terms of prices, output, innovation and quality and diversity of products and services”, *supra* note **Error! Bookmark not defined.**, Para 18; however, in its Annual Report 1971, the Commission considered that more objective information, such as the appellation, composition and specific purity of products and additives, shall be provided for the consumers, in order to adapt them to the changing situations, *supra* note **Error! Bookmark not defined.**, p199.

<sup>29</sup> Judgment of 7 June 2006, *Österreichische Postsparkasse AG and Bank für Arbeit und Wirtschaft AG v Commission*, T-213/01 and T-214/01, ECR, ECLI:EU:T:2006:151, Para 115.

<sup>30</sup> Judgment of 27 September 2006, *GlaxoSmithKline Services Unlimited v Commission*, T-168/01, ECR, ECLI:EU:T:2006:265, Para 118 and 171.

<sup>31</sup> Katalin Judit Cseres, *Competition Law and Consumer Protection* (Kluwer Law International, 2005), p245.

<sup>32</sup> Simon Bishop and Mike Walker, *Economics of EC Competition Law: Concepts, application and measurement* (Sweet & Maxwell, 1999), p5.

<sup>33</sup> Massimo Motta, *Competition policy, Theory and Practice* (Cambridge University Press, 2004), p15.

<sup>34</sup> Giorgio Monti, ‘Article 81 and public policy’, (2002) 39(5) *Common Market Law Review* 1057, pp.1057-1064.

<sup>35</sup> Christian Ahlborn and A. Jorge Padilla, ‘From fairness to welfare: implications for the assessment of unilateral conduct under EC competition law’, in Claus-Dieter Ehlermann and Mel Marquis (eds.) *European Competition Law Annual 2007: A Reformed Approach to Article 82 EC* (Hart Publishing, 2008), p61. According to this working paper, fairness goals cover fairness, the protection of economic freedom, the protection of rivalry and the competitive process and the protection of small and medium-size firms.

<sup>36</sup> Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights* (second edition, Oxford University Press, 2011), p25.

<sup>37</sup> Emil Paulis, ‘Abuses of Dominant Position and Monopolization: Conclusions of the Major Debates in the EU and USA’, in Abel M. Mateus and Teresa Moreira (eds.) *Competition Law and Economics: Advances in Competition Policy Enforcement in the EU and North America* (Edward Elgar, 2010), p162.

could be considered an objective of Article 102 TFEU or the EU competition regime,<sup>38</sup> and maintains that the protection of competitors in itself is not an objective.<sup>39</sup> It therefore seems that generally the scholars have recognized market integration, economic freedom, efficiency, and consumer welfare. While the former two objectives could be defined as traditional objectives, the latter two objectives are cutting-edge ones which also have to do with the evaluation of ostensibly abusive conduct.<sup>40</sup>

### **2.1.1 Market integration & economic freedom**

Market integration is one of the fundamental objectives of EU competition law and therefore has always been the Commission's most important concern.<sup>41</sup> It has been admitted in the White Paper that "at the beginning the focus of [the Commission's] activity was on establishing rules on restrictive practices interfering directly with the goal of market integration."<sup>42</sup> EU Competition rules are established to wipe out the obstacles to trade between member states deriving from the anti-competitive agreements and abusive conducts. The provisions of Article 101 and 102 TFEU are complementary to the four free movements. Realization of market integration is only possible when a set of tools comprising of free movement provisions and competition rules work well.

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<sup>38</sup> Thomas Eilmansberger, 'How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses' (2005) 42 *Common Market Law Review* 129, p136.

<sup>39</sup> *ibid*, p138.

<sup>40</sup> Josef Drexler, 'The Relationship between the Legal Exclusivity and Economic Market Power' in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, p28.

<sup>41</sup> See for instance the Speech of Commissioner Joaquín Almunia, 'Competition and consumers: the future of EU competition policy' European Competition Day, Madrid, 12 May 2010, SPEECH/10/233, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/10/233&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 1 Oct 2011, "the single market is one of the driving forces of the Europe 2020 strategy to achieve a new period of sustainable growth and buoyancy in the European Union. ... Competition helps to reinforce the single market. It removes barriers to trade in goods and services and it fosters innovation and competitiveness, which are fundamental to the goals of sustainable growth, environmental protection and social cohesion contained in the Europe 2020 strategy."; Speech of Director-General for Competition Alexander Italianer, 'Prepared remarks on: Level-playing field and innovation in technology markets', at Conference on Antitrust in Technology, Palo Alto (US), 28 Jan 2013, available at [http://ec.europa.eu/competition/speeches/text/sp2013\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2013_01_en.pdf), last visited on 19 Feb 2013, "[i]n Europe, the importance of preserving competition as a pre-condition for the success of the EU Single Market has been recognised from the start. This is why the Commission has been entrusted with a key mission of safeguarding competition in the Single Market" (p7).

<sup>42</sup> Commission White Paper on Modernization of the Rules Implementing Article 85 and 86 of the EC Treaty [1999] OJ C132/1, executive summary Para 8.

Likewise, from early time protection of economic freedom has been associated with the goal to construct a better internal market. While the objective of market integration would be realized by prohibiting anti-competitive agreements and abusive practices, the protection of individual economic freedom allows undertakings in the marketplace to conclude agreements or to adopt their commercial strategies at their own discretion. It is the undertakings' legitimate interest that they shall feel free to operate their business. Public power is not expected to step into the markets as long as the competitive process has not been or is unlikely to be distorted. For refusal to license cases, on the one hand, unless under exceptional circumstances dominant undertakings' economic freedom of adopting refusal decisions shall be protected from the competition authorities' intervention; on the other hand, the competitors' economic freedom of not being limited or eliminated from related market is also under protection to a certain degree.<sup>43</sup> Safeguarding the rivalry based on 'competition on the merits' in order to preserve the effective competition on related markets, namely balancing the interest of dominant undertakings and the interest of the whole industries, is one factor which is often cited to distinct the EU and the US competition regimes.<sup>44</sup>

### 2.1.2 Consumer welfare & Economic efficiency

#### (1) Consumer welfare: the ultimate objective

"[O]ur ultimate objective is: competition policy is a tool at the service of consumers. *Consumer welfare* is at the heart of our policy and its achievement drives our priorities and guides our decisions...Our objective is to ensure that consumers enjoy the benefits of competition, a wider choice of goods, of better quality and at lower prices."<sup>45</sup>

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<sup>43</sup> E.g. a dominant undertaking with a market position approaching that of a monopoly, or with a similar level of market power, is highly unlikely capable to justify its exclusionary conduct as the Commission considers remaining competitive pressure from the competitors is essential. See Communication from the Commission – *Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings*, [2009] OJ C45/7 (Hereinafter 'Commission Guidance'), Para 30(4); see also *DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses*. (Hereinafter 'Discussion Paper'), available at <http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf>, last visited on 10 Sep 2011. The comments received are available at <http://ec.europa.eu/competition/antitrust/art82/contributions.html>, Para 90, 91.

<sup>44</sup> See e.g. Dieter De Smet, 'The diametrically opposed principles of US and antitrust policy', (2008) 29(6) *European Competition Law Review* 356, pp.357-358; Roberto Pardolessi and Andrea Renda, 'The European Commission's Case Against Microsoft: Kill Bill?' (2004) 27(4) *World Competition* 513, p565.

<sup>45</sup> Speech of Commissioner Joaquín Almunia, 'Competition and consumers: the future of EU competition policy' European Competition Day, Madrid, 12 May 2010, SPEECH/10/233, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/10/233&format=HTML&aged=0&language=E>

It has been commonly acknowledged that consumer welfare is the main driver for competition policy. As the statement above, Joaquín Almunia has attached great importance to the consumer welfare and put it at the central place of competition policy. Former Director-General of the Competition DG Philip Lowe similarly maintains that competition policy institutions must ensure that “consumers are not harmed by anti-competitive agreements, exclusionary and exploitative conduct by one or more dominant undertakings”.<sup>46</sup> Sir John Vickers, former Chairman of Office of Fair Trading, describes the relation between consumer welfare and competition policy in this way, “[g]ood consumers and competition policies have one and the same goal – to help market work well for consumers and for the fair-dealing enterprises that serve consumers well.”<sup>47</sup>

Consumer welfare has been increasingly valued; however, it is not a wholly new concept. Since 1960s the upswing of the *consumerism* has brought Europe the concept of consumer welfare.<sup>48</sup> Under the formalistic structure-based approach, consumer welfare – the prominent objective nowadays – could be regarded as a by-conduct of the protection of competition. Article 102(b) TFEU forbids unilateral abusive conducts which are to the prejudice of consumers, however, the Treaty was considered to be infringed only if such conducts cause negative effects on the competitive process and then detrimental to consumers is automatically satisfied. Insufficient attention was directly paid to the effect on the consumer welfare. This was supported by Advocate General Kokott’s opinion in *British Airways* case<sup>49</sup>, in which it was believed that intervention is justified when there is harm to competitive process, rather than in the situation where direct or indirect harm to the consumers has been incurred:

“Article [102 TFEU], like the other competition rules of the Treaty, is not designed only or primarily to protect the immediate interests of individual competitor or consumers, but to protect the structure of the market and thus competition as such (as an institution), which has already been weakened by the presence of the dominant undertaking on the market. In this way, consumers are also indirectly protected. Because where competition as such is damaged, disadvantage for consumers are also to be feared”.<sup>50</sup>

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[N&guiLanguage=en](#), last visited on 1 Oct 2011. (emphasis added).

<sup>46</sup> Philip Lowe, ‘The design of competition policy institutions for the 21<sup>st</sup> century – the experience of the European Commission and DG Competition’, (2008) 3 *Competition Policy Newsletter* 1, p6.

<sup>47</sup> Sir John Vickers, opening remarks at the European Competition and Consumers Day Conference London, 15 September 2005, available at [http://ec.europa.eu/competition/publications/cpn/2005\\_3\\_49.pdf](http://ec.europa.eu/competition/publications/cpn/2005_3_49.pdf), last visited on 12 Dec 2011.

<sup>48</sup> Katalin Judit Cseres, *Competition Law and Consumer Protection* (Kluwer Law International, 2005), p160.

<sup>49</sup> Judgment in *British Airways*, C-95/04 P, ECLI:EU:C:2007:166.

<sup>50</sup> Ibid, Opinion of Advocate General Kokott, Para 68.

Consumer welfare has been the one placed in the process of Article 102 modernisation, which could be evidenced by the statement of Neelie Kroes<sup>51</sup> and the EAGCP's report *An Economic Approach to Article 82 EC*<sup>52</sup>. A significant shift towards an effects-based approach is apparent both in the Discussion Paper and the Commission Guidance, which would examine the legitimacy of certain business practices according to their impacts on consumer welfare. The new enforcement approach, according to Joaquín Almunia, “focuses on preventing or putting an end to *consumer harm*, rather than protecting ‘competitors’” and bases competition investigations on “sophisticated economic analysis”, “a qualitative knowledge of the market realities” and “a good understanding of *customer demands*”.<sup>53</sup>

However, while the focus on the consumer welfare has never been such greater, concern arises on the uncertain boundary of this objective. Is the consumer welfare simply equal to lower prices and better quality? For the EU Commission's part, consumer welfare includes not only lowering prices, providing better quality and more choices for consumers; what's more, “the benefits of more dynamic efficiencies associated with innovation and increased productivity” should also be taken into consideration.<sup>54</sup> The causal relationship between consumer welfare and refusal to license lies in that consumer welfare could apparently be prejudiced in a direct manner because as a result of a refusal, either “certain products may not put on the market”, or

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<sup>51</sup> See e.g. speech of Neelie Kroes, ‘Competition policy and consumers of November’, at the Fordham Corporate Law Institute, Brussels, 16 November 2006, SPEECH/06/691, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/06/691&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 11 Aug 2011. (“Whether we are looking at the actions of dominant companies, breaking up cartels, vetting mergers, or approving State aid – the potential harm to consumers is at the heart of what we do. We are applying this ‘consumer welfare standard’ through better use of economic analysis in our work.”)

<sup>52</sup> See the Economic Advisory Group for Competition Policy's report *An Economic Approach to Article 82 EC* (July 2005), available at [http://ec.europa.eu/dgs/competition/economist/eagcp\\_july\\_21\\_05.pdf](http://ec.europa.eu/dgs/competition/economist/eagcp_july_21_05.pdf), last visited on 17 Sep 2011. (“An economic approach to Article [102] focuses on improved consumer welfare. In so doing, avoids confusing the protection of competition with the protection of competitors and it stresses that the ultimate yardstick of competition policy is in the satisfaction of consumer needs.” p2)

<sup>53</sup> Speech of Commissioner Joaquín Almunia, ‘The road ahead International Forum on EU Competition Law’, Brussels, 9 March 2010, SPEECH/10/81, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/10/81&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 1 Oct 2011. (emphasis added)

<sup>54</sup> Speech of Neelie Kroes, Opening address at conference *Competition and Consumers in the 21st century* Brussels, 21st October 2009, SPEECH/09/486, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/09/486&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 1 Oct 2011.

“these products may not have to face the innovative competition from third party”;<sup>55</sup> the consumer welfare would also be jeopardized in an indirect way if the dynamic competition in the entire industry is impeded due to the refusal to license.

## (2) Dynamic & static efficiency

Consumer welfare and economic efficiency are often referred together, hence it is difficult to make a completely distinction between them.<sup>56</sup> Neelie Kroes held that Commission’s protection of competition serves as an instrument for achieving the aim of “enhancing consumer welfare and ensuring an efficient allocation of resources” and “an effects-based approach, grounded in solid economics, ensures that citizens enjoy the benefits of a competitive, dynamic market economy”.<sup>57</sup> However, it appears surprisingly that the Commission Guidance in its opening statement does not explicitly regard consumer welfare and efficiency as legal objectives of Article 102 TFEU, while the corresponding Article 101 TFEU and merger guidelines incorporate them as the ultimate goals.<sup>58</sup>

From the perspective of the competition law, the primary concern of *ex post* public intervention is *static* efficiency (allocative efficiency), namely competition *in* the market to offer consumers products with lower prices and better quality; IPR *inter alia* in those dynamically competitive industries<sup>59</sup> ask for more protection on *dynamic* efficiency, namely competition *for* the market, such as *ex ante* incentives to innovate.<sup>60</sup> Consumer welfare is not only influenced by the static

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<sup>55</sup> Floris O.W. Vogelaar, ‘The Compulsory Licence of Intellectual Rights under EC Competition Rules: an analysis of the exception to the general rule of ownership immunity from competition rules’, (2009) 6(1) *The Competition Law Review* 117, p134.

<sup>56</sup> Consumer welfare and efficiency are not only the objectives of EU competition law, but also have to do with the assessment of potentially abusive practice. More discussion see chapter 3 on *Microsoft I* case.

<sup>57</sup> Speech of Neelie Kroes, ‘European Competition Policy – Delivering Better Markets and Better Choices’, at European Consumer and Competition Day, London, on 15 September 2005, SPEECH/05/512, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/05/512&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 28 Aug 2011.

<sup>58</sup> See Guidelines on the application of Article 81(3) of the Treaty, [2004] OJ C 101/97, Para 13; Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, [2004] OJ C 101/2, Para 5; Guidelines on Vertical Restraints, [2010] OJ C 130/1, Para 7; Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, [2004] OJ C 31/5, Para 8; Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, [2008] OJ C 265/6, Para 10.

<sup>59</sup> Detailed discussions on dynamically competitive industries see *infra section* ‘4.2.2 Dominance in ‘dynamically competitive industries’.

<sup>60</sup> Kelvin Hiu Fai Kwok, ‘A New Approach to Resolving Refusal to License Intellectual Property Rights Disputes’, (2011) 34(2) *World Competition* 261, p263; Marcus Glader, *Innovation Markets and Competition Analysis: EU*

efficiency, on which the EU Commission and the European Court of Justice have traditionally focused; it is also positively affected by the dynamic efficiency, such as the incentives of the dominant undertaking to innovate as well as its competitors particularly in refusal cases.<sup>61</sup> Therefore, in which way consumer welfare is protected could be detected from how the competition authorities and courts strike the balance between *ex ante* and *ex post* efficiencies. Compared with dynamic efficiency, static efficiency has been emphasized, or even over-emphasized by the EU, which might be problematic particularly in dynamically competitive industries.<sup>62</sup> Such an undue emphasis is due to the reason that the benefits of *ex post* efficiency are easier to measure than those of *ex ante* efficiency.<sup>63</sup> It is apparent that the allocative gains, such as increased competition in the downstream market between different brands due to an order to license, is significant and identifiable in the short term, while it might be a formidable task to quantify the long term benefits on the other hand.<sup>64</sup>

Balancing *ex ante* and *ex post* efficiencies is a very difficult process. Many unpredictable factors have to be taken into consideration, which would probably result in false decisions. Thus, some scholars propose to substitute the original balancing test by comparing the welfare losses of the error of ‘false non-intervention’ and the error of ‘false intervention’ to discover which loss is relatively less.<sup>65</sup> The former error results in less competition *in* the market and hence a loss in allocative efficiency, while the latter error would cause less competition *for* the

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*Competition Law and US Antitrust Law* (Edward Elgar 2006), pp.56-57, 83-84.

<sup>61</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, p28.

<sup>62</sup> *ibid.* more discussion on dynamically competitive industries see chapter 2, section 4.2.2.

<sup>63</sup> See e.g. Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ (2004) 41 *Common Market Law Review* 1519, p1540; Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, p18.

<sup>64</sup> Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ (2004) 41 *Common Market Law Review* 1519, fn 76; Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, p18.

<sup>65</sup> See e.g. David S. Evans and A Jorge Padilla, ‘Designing Antitrust Rules for Assessing Unilateral Practices, A Neo-Chicago Approach’, (2005) 72 *University of Chicago Law Review* 73; Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>.

market and lower the general level of innovation. Competition law enforcers, according to these scholars, should not intervene in IPR cases since the efficiency loss from a ‘false intervention’ is much more significant than the potential welfare loss by a ‘false non-intervention’.<sup>66</sup> However, Drexel put forward his opposite opinion against this alternative approach, mainly arguing that this approach bases the prediction on the likely effects of a potential decision, elements of which are mostly unknown or unpredictable.<sup>67</sup> Moreover, the assumption that IPR always produces advantage in the sense of dynamic efficiency, on which this approach relies, according to Drexel’s conclusion, is not irrebuttable as “exaggerated protection can foreclose markets to competitors who might be more innovative than incumbent right holders”.<sup>68</sup> It appears that either the original balancing of *ex ante* and *ex post* efficiencies, or this alternative approach of comparing the welfare losses of two possible errors, should be applied with caution. One commentator concludes that such balancing should be applied in IP licensing scenario only for the purpose of examining whether the costs of compulsory license do not obviously outweigh the *ex post* gains.<sup>69</sup>

### 2.1.3 Multiple and (potentially) conflicting objectives in the AML

Article 1 of the AML sets forth that the purpose of the law is to “prevent and curb monopolistic conducts, protect fair market competition, enhance economic efficiency, maintain the consumer interests and the public interests, and promote the healthy development of socialist market economy”.<sup>70</sup> The multiple objectives explicitly listed in this article would make foreign investors feel like in an EU-like legal environment which they are familiar with.<sup>71</sup> A Chinese competition law scholar considers prohibiting monopolistic conducts and protecting fair market competition are direct objectives pursued by the AML, and economic efficiency, consumer welfare, public interests, and the healthy development of the socialist market economy are the ultimate objectives.<sup>72</sup>

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<sup>66</sup> *ibid.*

<sup>67</sup> Josef Drexel, ‘The Relationship between the Legal Exclusivity and Economic Market Power’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, pp.28-29.

<sup>68</sup> *ibid.*, p29. See more discussions on the relationship between the degree of IPR protection and the dynamic efficiency (such as the incentive to innovate) also in chapter 3.

<sup>69</sup> Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ 41 (2004) *Common Market Law Review* 1519, p1943.

<sup>70</sup> AML, *supra* note 9, Article 1.

<sup>71</sup> Maher M Dabbah, ‘The Development of Sound Competition Law and Policy in China: An (Im)possible Dream’, (2007) 30(2) *World Competition* 341, p355.

<sup>72</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The*



The commonalities between China's AML and the EU competition law could be reflected in their efforts spent on public policy considerations such as employment rate and social stability, instead of a "laissez-faire market economy".<sup>73</sup> However, the non competition-related objectives – 'public interests' and 'healthy development of the socialist market economy' – are rather ambiguous, causing uncertainty in implementing the law.<sup>74</sup> Take 'public interests' for example, from Article 1 of the AML it appears that it is not a synonym of 'consumer interests'. Article 15 of the AML stipulates that anticompetitive agreements could be exempted from the competition liability if the party to the agreement could demonstrate that the agreement concluded is for the 'public interests', such as for energy saving, environment protection or disaster relief.<sup>75</sup> The 'public interests', by these three examples enumerated in Article 15, thus might be interpreted as the national interests of the Chinese people, or the collective interests of the Chinese people in a substantial part of China. Then a question arises whether 'public interests' could, in some cases, be represented, or even be replaced by the interests of state-owned enterprises ('SOEs').<sup>76</sup>

The multi-objectives pursued by the AML do not merely raise the concern of definition problem. Moreover, multiple objectives require competition authorities or courts to conduct a delicate balance between different economic, social and political goals in particular cases in order to avoid potential conflict. In the EU, it is also difficult to avoid the conflict between competition related goals and other industrial policy considerations.<sup>77</sup> In a (limited) number of cases, the EU Commission has considered public policy goals, such as environmental goals, cultural policy goals, the protection of public health and consumers, employment policy and other industrial policy goals.<sup>78</sup> The CJEU has also acknowledged the broad discretion enjoyed

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*Antitrust Bulletin* 579, p584.

<sup>73</sup> Jacob S. Schneider, 'Administrative Monopoly and China's New Anti-Monopoly Law: Lessons from Europe's State Aid Doctrine' (2010) 87 *Washington University Law Review* 869, p889.

<sup>74</sup> See Mark Furse, 'Competition Law Choice in China', (2007) 30(2) *World Competition* 323, pp.334-335; Xiaoye Wang and Jessica Su, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar Publishing 2012) 379, p383.

<sup>75</sup> AML, *supra* note 9, Article 15.

<sup>76</sup> See Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133, pp142-143.

<sup>77</sup> See Xiaoye Wang and Jessica Su, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar 2012) 379, pp.393-394.

<sup>78</sup> Heike Schweitzer, 'Competition Law and Public Policy: Reconsidering an Uneasy Relationship. The Example of Art. 81' (2007) *EUI Working Papers Law* 2007/30, pp.6-7, available at <http://cadmus.eui.eu/bitstream/handle/1814/7623/LAW-2007-30.pdf?sequence=3>, last visited on 2 January 2014.

by the Commission to strike a proper balance between competition goals with public interest goals.<sup>79</sup> However, in the situations where the competition authority has to simultaneously take into account conflicting competition objectives and industrial objectives, more attention has been paid to the former.<sup>80</sup> As to the situation in China, in the absence of sufficient guidance, competition enforcement authorities, as well as the courts, will be confronted with contradictory instructions.<sup>81</sup> For example, ‘public interests’ might conflict with the AML’s another objective of improving consumer welfare.<sup>82</sup> Article 15 and Article 28 of the AML respectively provide that the anticompetitive agreements and concentrations could be exempted if the allegedly anti-competitive agreement or concentration at issue is for the purpose of achieving the public interests.<sup>83</sup> Thus, consumer interests and public interests might not be parallel under such circumstance.<sup>84</sup> According to decisions released so far by the competition authorities and Chinese courts, in practice there has been no such an anti-monopoly case – either in the public enforcement of the AML or in private lawsuits – where it has been further clarified how to balance these potentially conflicting objectives.

#### **2.1.4 Socialist market economy, SOEs and abuse of administrative power**

As a third way in between central-planned economy and laissez faire market economy, it is stated in the Treaty on the European Union that the internal market shall work for “a highly competitive social market economy”.<sup>85</sup> The ‘social market economy’ is literally very close to

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<sup>79</sup> See e.g. Judgment in *Metro*, 26/76, ECLI:EU:C:1977:167, Para. 21 (“The powers conferred upon the Commission under Art. 85(3) show that the requirements for the maintenance of workable competition may be reconciled with the safeguarding of objectives of a different nature and that to this end certain restrictions on competition are permissible, provided that they are essential to the attainment of those objectives and that they do not result in the elimination of competition for a substantial part of the common market.”); Judgment of 11 July 1996, *Metropole télévision SA v. Commission*, T-528/93, T-542/93, T-543/93 and T-546/93, ECR, ECLI:EU:T:1996:99, Para 118 (“in the context of an overall assessment, the Commission is entitled to base itself on considerations connected with the pursuit of the public interest in order to grant exemptions under Art. 81(3).”)

<sup>80</sup> See Xiaoye Wang and Jessica Su, ‘China’s Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy’ in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar 2012) 379, p394.

<sup>81</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, ‘Antitrust in China: The Problem of Incentive Compatibility’ (2005) 1(1) *Journal of Competition Law and Economics* 123, p142.

<sup>82</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p585.

<sup>83</sup> AML, *supra* note 9, Article 15 and 28.

<sup>84</sup> See Xiaoye Wang, ‘Highlights of China’s New Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 133, pp.143-144; Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, pp.585-586; Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, p251.

<sup>85</sup> *Consolidated version of the Treaty on European Union*, OJ C 326/13, 26 October 2012, Article 3(3). It is

the concept of ‘socialist market economy’ in Article 1 of the AML in the sense that they share a similar goal of developing a market economy while emphasizing also social needs such as social justice and distributive fairness.<sup>86</sup> However, these two concepts focus on quite different areas. The notion of ‘social market economy’ embraces social policy considerations into market freedom in the EU. The CJEU has in a number of cases stated that the Union has “not only an economic but also a social purpose”, and that the social policy objectives should also be taken into consideration.<sup>87</sup> Unlike EU’s ‘social market economy’, China’s ‘socialist market economy’ is an ideological concept. Unlike the countries in Eastern Europe where political and economic reforms took place at the same time, China is switching from a central-planned economy to a market economy while its political structure remains almost unchanged.<sup>88</sup> The notion of ‘socialist market economy’ was put forward by the Chinese Communist Party in its Fourteenth Meeting in 1992<sup>89</sup>, and was incorporated in the *1993 Amendment to the Constitution of the People’s Republic of China*.<sup>90</sup> The essence of the concept ‘socialist market economy’ is the leading position of the public ownership in the state economy.<sup>91</sup>

The AML in Article 4 states that “[t]he State formulates and implements competition rules compatible with the socialist market economy, improves the macro regulation and control, and

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beyond the scope of this chapter to discuss EU’s ‘social market economy’ in detail, see generally Alfred Müller-Armack, ‘The Social Market Economy as an Economic and Social Order’ (1978) 36(3) *Review of Social Economy* 325; Giorgio Monti, ‘EU Competition Law from Rome to Lisbon – Social Market Economy’ in Heide-Jorgensen *et al* (eds) *Aims and Values in Competition Law* (forthcoming), the article is available at <http://www.eui.eu/Documents/DepartmentsCentres/Law/Professors/Monti/GiorgioMonti-Cph-AimsandValuesinCompetitionLaw.pdf>, last visited on 20 January 2014; Christian Joerges and Florian Rodl, “Social Market Economy” as Europe’s Social Model’ *EUI Working Paper*, 2004/8.

<sup>86</sup> See David J. Gerber, ‘Constructing Competition Law in China: The Potential Value of European and U.S. Experience’ (2004) 3 *Washington University Global Studies Law Review* 315, pp.327-328.

<sup>87</sup> See e.g. Judgment in *Gabrielle Defrenne v Société anonyme belge de navigation aérienne Sabena*, 43/75, ECLI:EU:C:1976:56, Para 10; Judgment in *International Transport Workers’ Federation and Finnish Seamen’s Union v Viking Line ABP and OÜ Viking Line Eesti.*, C-438/05, ECLI:EU:C:2007:772, Para 79; Judgment in *Laval un Partneri Ltd v Svenska Byggnadsarbetareförbundet, Svenska Byggnadsarbetareförbundets avdelning 1, Byggettan and Svenska Elektrikerförbundet*, C-341/05, ECLI:EU:C:2007:809, Para 105.

<sup>88</sup> See Yong Huang, ‘Pursing the Second Best: The History, Momentum, and Remaining Issues of China’s Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 117, p118.

<sup>89</sup> See Zhenguo Wu, ‘Perspectives on the Chinese Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 73, p74.

<sup>90</sup> *Constitution of the People’s Republic of China* (adopted by the National People’s Congress in 1982, amended in 1988, 1993, 1999 and 2004), translation available by subscription at <http://www.lawinfochina.com/Display.aspx?Lib=law&Id=3437&keyword=>, last visited on 13 December 2013, Article 6.

<sup>91</sup> *Ibid.*

strengthens a unified, open, competitive and orderly market system.” As one main competition enforcement authority, the Ministry of Commerce (‘MOFCOM’) has also made it clear that realisation of other objectives, such as economic efficiency, cannot violate the public ownership principle.<sup>92</sup> It then inevitably raises concern by both Chinese and foreign commentators that industrial policy may be unduly emphasized in the implementation of the competition law.<sup>93</sup> Chinese commentators believe that, given the current political structure and legal condition in China, when there are conflicting industrial policy considerations in individual cases, competition goals would not be given a superior position like advanced economies such as the EU, the US and Germany, and compromise may be unlikely to avoid.<sup>94</sup>

With respect to the position of the AML in terms of the state-owned enterprises (‘SOEs’), Article 7 of the AML states that “[w]ith respect to the industries controlled by the State-owned economy and concerning the lifeline of national economy and national security or the industries lawfully enjoying exclusive production and sales, the State shall protect these lawful business operations conducted by the business operators therein, and shall supervise and control these business operations and the prices of these commodities and services provided by these business operators, so as to protect the consumer interests and facilitate technological advancements.” This article provides no meaningful guidance in striking the balance between AML enforcement in favour of Chinese consumers and the commercial interests of the SOEs, nor exemption for the SOEs.<sup>95</sup>

Socialist market economy and the SOEs could also be related to the administrative monopoly issue, or ‘abuse of administrative power’ which is prohibited by the AML. The China’s economic reform since 1978 has resulted in decentralized administrative system by which local and provincial governments have attained much control of the economy.<sup>96</sup> The essence of the administrative monopoly is local governments’ discriminatory behaviour that aims to protect

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<sup>92</sup> See Shang Ming (ed.), *The Anti-Monopoly Law of the People’s Republic of China: Interpretations and Application* (Lawpress, China, 2007), p16; Yong Huang, ‘Pursing the Second Best: The History, Momentum, and Remaining Issues of China’s Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 117, p120.

<sup>93</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, pp.585-586; Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, pp.95-96.

<sup>94</sup> See Xiaoye Wang and Jessica Su, ‘China’s Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy’ in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar 2012) 379, pp.394-396.

<sup>95</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p114; Zhenguo Wu, ‘Perspectives on the Chinese Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 73, p99.

<sup>96</sup> See Jacob S. Schneider, ‘Administrative Monopoly and China’s New Anti-Monopoly Law: Lessons from Europe’s State Aid Doctrine’ (2010) 87 *Washington University Law Review* 869, pp.872-874.

local undertakings, *inter alia* the SOEs located in that region, and has the effect of impeding the establishment of a unified, open and competitive nationwide market.<sup>97</sup> Local protectionism, resulting from administrative monopoly, is perceived to be most serious obstacle in implementing competition rules in China.<sup>98</sup> Such undue protection on the SOEs has been argued to be responsible for poor products and services delivered for consumers.<sup>99</sup> The fact that the ‘abuse of administrative power’ section in the AML draft was completely deleted and resumed for several times in the legislative process may demonstrate the wrestling between creating a level playing field for all market participants and maintaining the leading position of SOEs in China.<sup>100</sup> Although the chapter prohibiting abuse of administrative power remains in the final AML, the competition authorities are not empowered to enforce the AML against administrative power abuse.<sup>101</sup> According to the AML, administrative organ or organization’s abusive practice could only be corrected by their superior authorities, who are however unlikely to be well-trained to rectify the abuse of administrative power.<sup>102</sup> Apart from the lacking of sufficient competition law-related knowledge to curb administrative monopoly, the willingness of the superior authority to remain impartial between its subordinates and unsatisfied undertakings has raised scepticism as well.<sup>103</sup> Within the AML enforcement regime<sup>104</sup>, it is

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<sup>97</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, pp.595-596.

<sup>98</sup> See e.g. Xianchu Zhang, ‘An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy’ (2009) 43 *The International Lawyer* 1469, p1470.

<sup>99</sup> Grace Li and Angus Young, ‘Competition Laws and Policies in China and Hong Kong: A Tale of Two Regulatory Journeys’ (2008) 7 *Journal of International Trade Law and Policy* 186, available at SSRN: <http://ssrn.com/abstract=1421792>, last visited on 13 December, p7.

<sup>100</sup> Xianchu Zhang, ‘An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy’ (2009) 43 *The International Lawyer* 1469, p1480.

<sup>101</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p119. See also Mark William, Chapter 4 ‘China’ in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p110.

<sup>102</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p596. Article 51 of the AML provides that: “[w]here an administrative organ or organization empowered by law or administrative regulation to administer public affairs abuses its administrative power to eliminate or restrict competition, the superior authority thereof shall order the agency to make rectification and impose punishments on the directly responsible persons in charge and the other directly liable persons. The Anti-monopoly Law Enforcement Agency *may offer suggestions* to the relevant superior authority regarding how to handle the abuse according to law.” (*supra* note 9, emphasis added)

<sup>103</sup> See NPC Standing Committee member Lin Qiang’s opinion in the NPC published select excerpts of the discussion on the AML draft, 24 August 2007, available at [http://www.npc.gov.cn/npc/zq/2007-09/06/content\\_371692.htm](http://www.npc.gov.cn/npc/zq/2007-09/06/content_371692.htm), last visited on 28 December 2013, English translation see Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p120. (“Due to many reasons, sometimes it is very difficult for a supervising agency to break various

argued that the assignment of the Anti-monopoly Committee members to the representatives of different state ministries and agencies<sup>105</sup> has also served the socialist market economy, *inter alia* some regulated sectors.<sup>106</sup> Under such arrangement, the independence of the Committee could not be guaranteed, since such structure might pay too much attention on industrial policy considerations, causing potential conflict of interests considering the AML prohibits abuse of administrative power.<sup>107</sup>

One could find that, while limitations of the exercise of sovereignty have been imposed on local authorities' anticompetitive policymaking in the US and the EU, AML's prohibition on administrative monopoly has nothing to do with sovereignty.<sup>108</sup> Apart from this, the EU competition law could provide more guidance for China in this respect.<sup>109</sup> Since the early 1950s, the Europe has faced the problems of government influence on the market and regional protectionism.<sup>110</sup> Like the AML, the EU competition regime is designed for breaking down trade barriers, eliminating local protectionism, and establishing a unified market within the EU. The administrative monopoly provisions in the AML are similar to the situation in the EU in the sense that, aside from some exceptions, both regimes prohibit anticompetitive governmental interference in the market, while in the US state action doctrine has established an immunity for

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administrative monopolies. For example, first, behind any administrative monopoly lies some protection of local enterprises or economic motives, which makes it difficult for the supervising agency to remain impartial in disputes between its subordinates and other local enterprises. That is to say that the local protectionism or the protection of some departments might be prevalent within the supervising agency. Therefore, it is hard to curb administrative monopoly. Second, the supervising agency is not specified and, in practice, the personnel of the supervising agency are not necessarily strongly aware of antimonopoly and lack the ability to address and rectify such competition cases.”)

<sup>104</sup> See *infra* section 3.1.

<sup>105</sup> See *Notice of the General Office of the State Council on the Main Functions and Members of the Anti-Monopoly Commission of the State Council* (issued by the General Office of the State Council, effective on 28 July 2008, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7190&lib=law&SearchKeyword=&SearchCKeyword=%B9%FA%CE%F1%D4%BA%B7%B4%C2%A2%B6%CF%CE%AF%D4%B1%BB%E1>, last visited on 20 January 2014)..

<sup>106</sup> See Xianchu Zhang, ‘An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy’ (2009) 43 *The International Lawyer* 1469, p1479.

<sup>107</sup> *Ibid*, p1480.

<sup>108</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p118.

<sup>109</sup> See Jacob S. Schneider, ‘Administrative Monopoly and China’s New Anti-Monopoly Law: Lessons from Europe’s State Aid Doctrine’ (2010) 87 *Washington University Law Review* 869, pp.888-895.

<sup>110</sup> See Eleanor M. Fox, ‘An Anti-Monopoly Law for China – Scaling the Walls of Government Restraints’ (2008) 75 *Antitrust Law Journal* 173, p186; Claus-Dieter Ehlermann, ‘State Aids under European Community Competition Law’ (1994) 18 *Fordham International Law Journal* 410, pp.414-416.

the states regarding the antitrust law and state interference is thus generally allowed.<sup>111</sup> Therefore, EU's state aid doctrine and its exemptions could provide an example for China in balancing the general prohibition of regional protectionism and the reservation of space for economic assistance in exceptional circumstances.<sup>112</sup>

## 2.2 Three pillars

### 2.2.1 Anticompetitive agreements

Apart from the objectives pursued by the jurisdictions, as will be demonstrated below, more similarities between the AML and corresponding EU competition rules could be observed with regard to the substantial provisions in the three competition law pillars – anticompetitive agreements, abuse of dominant position and concentration of economic entities. Like the EU competition law, the AML distinguishes between horizontal and vertical agreements between undertakings. As to the horizontal agreements, the AML prohibits competitors from reaching agreements, which “fix or change the price of products, restrict the production quantity or sales volume of products, divide the sales market or the raw material supply market, restrict the purchase of new technology or new facilities or the development of new technology or new products, jointly boycott transactions, or other restrictive agreements determined by the competition authorities”.<sup>113</sup> As to the vertical agreements, since they are not intrinsically restrictive, the AML mainly prohibits the practice of resale price maintenance.<sup>114</sup> Subsequent to the prohibition provisions, the AML provides an Article 101(3) TFEU-like exemption provision.<sup>115</sup> The prohibition shall not apply if the undertakings involved could prove that the agreements are for the purpose of “(1) improving technologies, researching, and developing new products; (2) upgrading product quality, reducing costs, improving efficiency, unifying product specifications or standards, or carrying out professional labour division; (3) enhancing operational efficiency and reinforcing the competitiveness of small and medium-sized business operators; (4) realizing public interests such as conserving energy, protecting the environment

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<sup>111</sup> See Jacob S. Schneider, ‘Administrative Monopoly and China’s New Anti-Monopoly Law: Lessons from Europe’s State Aid Doctrine’ (2010) 87 *Washington University Law Review* 869, p884; Julio Baquero Cruz, *Between Competition and Free Movement: The Economic Constitutional Law of the European Community* (Hart Publishing 2002), pp.127-128.

<sup>112</sup> See Jacob S. Schneider, ‘Administrative Monopoly and China’s New Anti-Monopoly Law: Lessons from Europe’s State Aid Doctrine’ (2010) 87 *Washington University Law Review* 869, p891.

<sup>113</sup> AML, *supra* note 9, Article 13, Para 1.

<sup>114</sup> *Ibid*, Article 14.

<sup>115</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p599. Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p146.

and providing disaster relief, etc.; (5) mitigating the severe decrease of sales volume or obviously excessive production during economic recessions; (6) protecting the justifiable interests of the foreign trade or foreign economic cooperation; or (7) other circumstances prescribed by the law or the State Council.”<sup>116</sup> Moreover, the undertakings should also prove that the agreements will not substantially eliminate competition and the benefits will pass onto the consumers.<sup>117</sup> However, unlike Article 101(3) TFEU, this exemption provision does not require that the restraints be *indispensable* to realising these purposes.<sup>118</sup> It should be noted that the *crisis cartel* exemption (indicated above as the fifth exemption) and *export cartel* exemption (indicated as the sixth exemption) – which are argued to significantly weaken the potential of the AML<sup>119</sup> – are respectively based on the previous German competition law<sup>120</sup> and the US *Webb-Pomerene Act of 1918*<sup>121</sup> and the *Export Trading Act of 1982*<sup>122, 123</sup>. In addition, the AML’s abandonment of the notification mechanism, which was adopted in the previous AML draft in 2004, demonstrates that the AML follows the model of EU Regulation 1/2003<sup>124</sup> in this regard.<sup>125</sup>

### 2.2.2 Abuse of dominant position

With regard to the provisions prohibiting abuse of dominant market position, this is a significant area where the AML and current US antitrust policy diverge.<sup>126</sup> The Chicago School perspective emphasizes and encourages the superior innovation and economic efficiency brought about by the large-scale enterprises, which finally benefit consumers.<sup>127</sup> But China’s abuse-of-dominance provisions, like the multiple objectives of the AML as demonstrated above,

<sup>116</sup> AML, *supra* note 9, Article 15, Para 1.

<sup>117</sup> *Ibid*, Article 15, Para 2.

<sup>118</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p146.

<sup>119</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p86.

<sup>120</sup> *Act against Restraints on Competition GWB*, chapter I §6 (1998), now abolished.

<sup>121</sup> 15 U.S.C. § 61-65. (2012)

<sup>122</sup> 15 U.S.C. § 4001-4003, 4011-4021. (2012)

<sup>123</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, pp.599-600.

<sup>124</sup> *Council Regulation No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Article 81 and 82 of the Treaty*, [2003] OJ L1/1.

<sup>125</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p601.

<sup>126</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, pp.65-74.

<sup>127</sup> *Ibid*, p67.



have been found by US commentators close to US antitrust policies of the 1940s through the 1960s which was prior to the Chicago School.<sup>128</sup> Or more precisely, as some European and Chinese scholars observed, the AML has adopted a model similar to the EU scheme of dominance abuse, including the most significant factors in reviewing abusive cases, for instance the definition of relevant market, the concept of a dominant market position, the relevant aspects in assessing a dominance position, specific prohibited abusive practices.<sup>129</sup>

What constitutes a dominant position for competition law purposes is a threshold question. A dominant position has been construed in EU competition law as “a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers.”<sup>130</sup> According to the AML, an undertaking is considered as holding a dominant position in relevant market if it possesses “the ability to control the price or quantity of commodities or other trading conditions in the relevant market, or block or affect the entry of other business operators into the relevant market.”<sup>131</sup> Though the definition of a dominant position in the AML appears to be, to some

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<sup>128</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p68.

<sup>129</sup> See Mark Furse, ‘Competition Law Choice in China’, (2007) 30(2) *World Competition* 323, p325; Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, pp.252, 255-256; Xiaoye Wang, ‘Highlights of China’s New Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 133, p134; Zhenguo Wu, ‘Perspectives on the Chinese Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 73, p85.

<sup>130</sup> See Judgment in *United Brands* ECLI:EU:C:1978:22, Para 65; Judgment in *Hoffmann-La Roche*, 85/76, ECLI:EU:C:1979:36, Para 38.

<sup>131</sup> AML, *supra* note 9, Article 17. As the two competition authorities that have jurisdiction over dominant undertaking’s abusive practice, the State Administration for Industry and Commerce (‘SAIC’) and the National Development and Reform Commission (‘NDRC’) have in their implementing rules more detailed definitions for some concepts or terms used in the AML. In SAIC’s *Provisions on the Prohibition of Abuse of Dominant Market Position* (adopted by the State Administration for Industry and Commerce, issued on 31 December 2010 and effective since 1 February 2011, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8540&lib=law&SearchKeyword=Prohibition%20of%20Abuse%20of%20Dominant%20Market%20Position&SearchCKeyword=>, last visited on 20 December 2013), Article 3 supplements that “other trading conditions” could be the factors which may substantially affect market transactions, including but not limited to product quality, payment terms, mode of delivery, after-sales service. As to the term “to block or affect the access of other business operators to the relevant market”, SAIC’s implementing rule considers that apart from the situation where access of other undertakings to the relevant market is eliminated, the undertaking investigated will also be regarded as possessing a dominant position if its market power enables it to prevent other undertakings from entering into the relevant market at a good time or entering into the market at the expense of a higher cost.

extent, more stringent than EU competition law,<sup>132</sup> it is largely similar to that developed by the EU.<sup>133</sup>

A number of factors on which the AML bases to establish the existence of a dominant position are akin to those in EU case law, such as in *Hoffmann-La Roche*<sup>134</sup>. Pursuant to the AML, the assessment of whether an undertaking is in a dominant position will take into account relevant factors, in particular the following: the market share of the undertaking, and the competitive structure of the relevant market; the market power of the undertaking on the sales market, or the input supply market; the financial and technological strength of the undertaking; the extent of dependence of other undertakings in the relevant market; the barriers to entry into the relevant market.<sup>135</sup>

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NDRC's *Provisions against Price Fixing* (adopted by the National Development and Reform Commission, issued on 29 December 2010 and effective since 1 February 2011, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8440&lib=law&SearchKeyword=Provisions%20against%20Price%20Fixing&SearchCKeyword=>, last visited on 20 December 2013) has almost the same definition for the concept of dominance. Article 17 of the *Provisions against Price Fixing* states that “[t]he term ‘dominant market status’ as mentioned in these Provisions means that a business operator has the ability to control the price or quantity of commodities or other trading conditions in the relevant market or to block or affect the access of other business operators to the relevant market. ‘Other trading conditions’ refer to other factors which may have a material impact on market transactions in addition to price or quantity of commodities, including the grade of commodities, payment terms, way of delivery, after service, *trading options*, *technical constraints*, etc. ‘To block or affect the access of other business operators to the relevant market’ means to eliminate or delay the access of other business operators to the relevant market or cause a significantly higher cost to other business operators which, though able to access the relevant market, cannot effectively compete with the existing business operators.” (emphasis added)

<sup>132</sup> See Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, pp.254-255.

<sup>133</sup> See Maher M Dabbah, ‘The Development of Sound Competition Law and Policy in China: An (Im)possible Dream’, (2007) 30(2) *World Competition* 341, p360. The definition of a dominant position in the AML is also believed to be similar to the US antitrust law definition of market power, see e.g. Xiaoye Wang, ‘Highlights of China’s New Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 133, p138; H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p214.

<sup>134</sup> Judgment in *Hoffmann-La Roche* ECLI:EU:C:1979:36, Para 36-49.

<sup>135</sup> AML, *supra* note 9, Article 18. With regard to the factors enumerated in the AML, while the NDRC in Article 18 of its *Provisions against Price Fixing* (*supra* note 131) merely duplicates AML’s provision, the SAIC in the *Provisions on the Prohibition of Abuse of Dominant Market Position* (*supra* note 131) provides more detailed explanations for each expression. Article 10 of SAIC’s implementing rule states that “[t]he following elements shall be taken into account in finding a business operator’s dominant market position:

1. The business operator’s market share and competitiveness in the relevant market. “Market share” refers to the sales volume, sales quantity and other measurements of a certain product of the business operator as a

To alleviate the difficulties in determining market dominance, the AML provides certain fast rules for assessing dominant position based on market shares. Any undertaking with a market share higher than fifty percent, or two undertakings with a combined market share higher than two thirds, or three undertakings with a combined market share higher than three fourths, will be presumed as possessing a dominant market position.<sup>136</sup> However, collective dominance should not be established if the market share of any undertaking involved is less than ten percent.<sup>137</sup> Undertakings concerned are allowed to rebut the presumption if solid evidences could be provided to demonstrate that they do not hold a dominant position even with a high market share.<sup>138</sup> However, there is no guidance in the AML on what evidence will suffice to rebut the dominance presumption. In the absence of further clarification, the competition authorities, or the courts, might arbitrarily establish a dominant position without regard to the particular nature of the relevant market and the constraints imposed by remaining competitors.<sup>139</sup> The AML's relying on market share is more akin to EU competition law. US antitrust law does not believe that it is "appropriate or helpful" to presume monopoly power

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percentage in the relevant market over a given period of time. A business operator's competitiveness in the relevant market shall be determined based on the development situation of the relevant market, the number and market share of existing competitors, product differences, potential competitors, etc.

2. The business operator's ability to control the sales market or material purchase market. A business operator's ability to control the sales market or material purchase market shall be determined based on its ability to control the sales or purchase channels, its ability to affect or decide the price, quantity, contract term or other trading terms of products and its ability to take precedence in acquiring raw materials, semi-finished products, components and facilities necessary for its production or operation activities.

3. The business operator's financial capacity and technical conditions. A business operator's financial capacity and technical conditions shall be determined based on its assets scale, financial capacity, earning power, financing capability, research and development ability, technical equipment, technical innovation and application ability, intellectual property it owns, etc. It is also necessary to take into account the financial capacity and technical conditions of parties related to the business operator.

4. Other business operators' reliance on the business operator. Other business operators' reliance on a business operator shall be determined based on the trading volume between the business operator and other business operators, duration of their trading relationships, difficulty in changing to other counterparties, etc.

5. Difficulty for other business operators to access the relevant market. The difficulty for other business operators to access the relevant market shall be determined based on the market access rules, equipment of necessary facilities, sales channels, capital, technical requirements, cost, etc.

6. Other factors concerning the finding of a dominant market position."

<sup>136</sup> AML, *supra* note 9, Article 19, Para 1.

<sup>137</sup> Ibid, Article 19, Para 2.

<sup>138</sup> Ibid, Article 19, Para 3.

<sup>139</sup> See H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, pp.223-224.

based solely on market share because different markets have unique characteristics.<sup>140</sup> Compared to the US antitrust law, high market share is more, sometimes even solely relied by EU competition law to find a dominant position.<sup>141</sup> Furthermore, to constitute a *high* market share, EU competition law uses a relatively lower threshold as the EU Commission may consider the existence of dominance when the market share of undertaking concerned is higher than 50 percent.<sup>142</sup> The threshold in the US is higher. The US antitrust official held that a market share of 50 percent is too low to generate monopoly power,<sup>143</sup> and the threshold found in the US case is around 80 percent.<sup>144</sup> Regarding the collective dominance provided in the Article 19 of the AML, it should be reminded that neither the EU competition law nor the US antitrust law bases multiple undertakings' jointly dominant position on their combined market shares.<sup>145</sup> According to US antitrust official, the scenario where collectively dominant undertakings agree to act in concert is the only one situation that would raise significant competition concern.<sup>146</sup> Thus, the presumptions of collective dominant position should be eliminated from the abuse-of-dominance provisions, and prohibitions against monopoly agreements should be relied on to address competitors' concerted actions.<sup>147</sup> In fact,

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<sup>140</sup> See e.g. Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p69; Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, 'Key Issues regarding China's Antimonopoly Legislation', remarks presented to the International Seminar on Review of Antimonopoly Law, Hangzhou, China, 19 May 2006, available at <http://www.justice.gov/atr/public/speeches/217612.htm>, last visited on 22 December 2013.

<sup>141</sup> See H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, p221. See also Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, fn30.

<sup>142</sup> Judgment in *Irish Sugar*, T-228/97, ECLI:EU:T:1999:246, Para 70.

<sup>143</sup> Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, 'Some Comments on the Abuse-of-Dominance Provisions of China's Draft Antimonopoly Law', remarks presented to the UIBE Competition Law Center Conference on Abuse of Dominance: Theory and Practice, Beijing, China, 21 July 2007, available at <http://www.justice.gov/atr/public/speeches/225357.htm>, last visited on 24 December 2013.

<sup>144</sup> *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451 (1992), at 481.

<sup>145</sup> See H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, p222; Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p70.

<sup>146</sup> See Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, 'Some Comments on the Abuse-of-Dominance Provisions of China's Draft Antimonopoly Law', remarks presented to the UIBE Competition Law Center Conference on Abuse of Dominance: Theory and Practice, Beijing, China, 21 July 2007, available at <http://www.justice.gov/atr/public/speeches/225357.htm>, last visited on 24 December 2013.

<sup>147</sup> *Ibid.*

the rebuttable presumptions are originally derived from German competition rules.<sup>148</sup> But at least the AML has embraced the EU concept of ‘collective dominant position’ held by two or more economic entities “legally independent of each other”<sup>149, 150</sup>

As to the specific practices, a non-exhaustive list of abusive conducts under Article 17 of the AML is modelled after Article 102 TFEU with minor differences.<sup>151</sup> However, from the perspective of US commentators, the AML prohibits a number of normal conducts which are lawful in the US.<sup>152</sup> As an US antitrust official put it:

“Refusals to deal, exclusive dealing, tying, and price discrimination all can be used for procompetitive, efficiency-enhancing reasons and in only very limited circumstances will have anticompetitive effects, even when used by a firm with a dominant market position. Indeed, practices such as these are very common in highly competitive markets, reflecting that such distribution methods can reduce costs and improve efficiency. Therefore, it is important that these practices not be presumed to be anticompetitive, either in the law or by the antimonopoly enforcement agency in implementing the law. These practices should be viewed as unlawful only if, after a detailed analysis of the conduct, the market, and proffered business justifications, it is determined that the conduct harms competition by creating, maintaining or strengthening the monopoly power of the dominant firm and that the conduct makes economic sense to the firm only because of its anticompetitive effects.”<sup>153</sup>

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<sup>148</sup> See *Act Against Restraints of Competition* in the version published on 15 July 2005 (Bundesgesetzblatt (Federal Law Gazette) I, page 2114; 2009 I page 3850), as last amended by Article 3 of the Act of 26 July 2011 (Federal Law Gazette I, page 1554), § 19(3), available at [http://shvv.juris.de/englisch\\_gwb/act\\_against\\_restraints\\_of\\_competition.pdf](http://shvv.juris.de/englisch_gwb/act_against_restraints_of_competition.pdf), last visited on 9 December 2013.

<sup>149</sup> Judgment in *Compagnie Maritime Belge Transports SA v. Commission*, C-395/96 P and C-396/96 P, ECLI:EU:C:2000:132, at 1458.

<sup>150</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p222.

<sup>151</sup> See Yin Zhou, ‘China’s Anti-Monopoly Law: Insights from U.S. and EU Precedents on Abuse of Dominance and IP Exemption Provisions’ (2009) 32(2) *Hastings International and Comparative Law Review* 711, p715; Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, p256.

<sup>152</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p65.

<sup>153</sup> Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, ‘Key Issues regarding China’s Antimonopoly Legislation’, remarks presented to the International Seminar on Review of Antimonopoly Law, Hangzhou, China, 19 May 2006, available at <http://www.justice.gov/atr/public/speeches/217612.htm>, last visited on 22 December 2013. In addition to these conducts, Masoudi also held that the AML enforcement authority should find predatory pricing in the narrow range

Take excessive pricing – one particular commercial practice where the EU competition law and the US antitrust law diverge<sup>154</sup> – for example, it is worth noting that, similar to Article 102(a), the AML prohibits dominant undertakings from “selling products at unfairly high prices or buying products at unfairly low prices”.<sup>155</sup> But according to the US official, it should not be unlawful for a dominant firm to charge a market-determined monopoly price for its products, because “the prospect of obtaining higher-than-normal profits” is essential for bringing incentives to the dominant firm and developing innovative products for final consumers.<sup>156</sup>

In respect of the sanctions against an abusive conduct, Chinese enforcement authorities are allowed by the AML to impose on the dominant undertaking a fine ranging from one percent to ten percent of the dominant undertaking’s turnover in the preceding year.<sup>157</sup> While the minimum amount of fines has been questioned to be disproportionate for minor infringements, the maximum amount of fines is somehow consistent with the rule in the EU.<sup>158</sup>

In addition to the fundamental provisions stipulated in the AML, in defining the relevant market, Anti-Monopoly Committee’s *Market Definition Guideline*<sup>159</sup> has adopted an

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of circumstances, since such inherently risky strategy “involves sacrificing real current profits for the very speculative possibility of recouping even more profits in the future”, which has been rarely seen. See also Gerald F. Masoudi, ‘Some Comments on the Abuse-of-Dominance Provisions of China’s Draft Antimonopoly Law’, remarks presented to the UIBE Competition Law Center Conference on Abuse of Dominance: Theory and Practice, Beijing, China, 21 July 2007, available at <http://www.justice.gov/atr/public/speeches/225357.htm>, last visited on 22 December 2013.

<sup>154</sup> See Chapter 4.

<sup>155</sup> AML, *supra* note 9, Article 17. In fact, EU competition authority does not actively pursue purely high pricing behaviour as abuse of dominance, see Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p150.

<sup>156</sup> Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, ‘Some Comments on the Abuse-of-Dominance Provisions of China’s Draft Antimonopoly Law’, remarks presented to the UIBE Competition Law Center Conference on Abuse of Dominance: Theory and Practice, Beijing, China, 21 July 2007, available at <http://www.justice.gov/atr/public/speeches/225357.htm>, last visited on 24 December 2013. In addition to the ‘unfairly high price’ prohibition, US scholars also hold that buying products at unfairly low prices is normal pricing practice which could be commonly found in a competitive market. See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p71.

<sup>157</sup> AML, *supra* note 9, Article 47.

<sup>158</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p151.

<sup>159</sup> *Guide of the Anti-Monopoly Committee of the State Council for the Definition of the Relevant Market* (issued and effective on 24 May 2009). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7575&lib=law&SearchKeyword=Definition%20of%20the%20Rele>

approach which is largely consistent with the practice in the EU as well.<sup>160</sup> Although the Committee's *Market Definition Guideline* is much less detailed with merely 11 articles, the most essential aspects in defining the relevant market – such as the definition of relevant market in both product and geographic dimensions,<sup>161</sup> the examination of competitive constraints arising from demand-side substitutability and supply-side substitutability,<sup>162</sup> the adoption of the SSNIP test<sup>163</sup> – closely follow well-established principles of market definition in the EU Commission's *Notice on the definition of relevant market*<sup>164</sup>.

### 2.2.3 Concentration

In addition to the Chinese version of Article 101 and 102 TFEU, the merger control provisions in the AML, besides some unique characteristics, are generally consistent with the EU rules.<sup>165</sup> Like the EU competition law, the AML defines reportable transactions as 'concentrations', which includes mergers, acquisitions of control of other undertakings by purchasing their equities or assets, and acquisitions of control or capability to exercise decisive influence on other undertakings by contract or other means.<sup>166</sup> Such definition of concentration derives from the EU Merger Regulation 139/2004<sup>167</sup>, as well as the German competition law<sup>168</sup>. Nevertheless, unlike the EU where "[t]he creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity shall constitute a concentration",<sup>169</sup> it has not been clarified in the AML whether and in which circumstances creation of joint ventures should be

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<sup>160</sup> See Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p255.

<sup>161</sup> *Guide for the Definition of the Relevant Market*, *supra* note 159, Article 3, 8 and 9.

<sup>162</sup> *Ibid*, Article 4-6.

<sup>163</sup> *Ibid*, Article 10. However, it should be reminded that SSNIP was firstly and is still adopted by the US Department of Justice in its Horizontal Merger Guidelines.

<sup>164</sup> *Commission Notice on the definition of relevant market for the purpose of Community Competition Law* [1997] OJ C 372/5.

<sup>165</sup> See Susan Beth Farmer, 'The Evolution of Chinese Merger Notification Guidelines: A Work in Progress Integrating Global Consensus and Domestic Imperatives' (2009) 18 *Tulane Journal of International and Comparative Law* 1, p9.

<sup>166</sup> AML, *supra* note 9, Article 20.

<sup>167</sup> *Council Regulation No 139/2004 of 20 January 2004 on the control of concentrations between undertakings*, [2004] OJ L 24/1, Article 3.

<sup>168</sup> See *Act Against Restraints of Competition* in the version published on 15 July 2005 (Bundesgesetzblatt (Federal Law Gazette) I, page 2114; 2009 I page 3850), as last amended by Article 3 of the Act of 26 July 2011 (Federal Law Gazette I, page 1554), § 37, available at [http://shvv.juris.de/englisch\\_gwb/act\\_against\\_restraints\\_of\\_competition.pdf](http://shvv.juris.de/englisch_gwb/act_against_restraints_of_competition.pdf), last visited on 9 December 2013.

<sup>169</sup> *EU Merger Regulation 139/2004*, *supra* note 167, Article 3(4).



reviewed as concentration rather than monopoly agreement. The MOFCOM draft *Interim Measures on the Notification of Business Operators' Concentration* stipulated that “the establishment of a new continuously and independently operating enterprise by two or more business operators (hereinafter parent companies) falls into the scope of concentrations of business operators as provided in Article 20 of the Anti-Monopoly Law”.<sup>170</sup> In a later draft released by the Legislative Affairs Office of State Council, it explicitly provided that the concentration rules should not apply to the establishment of “special purpose companies which only undertake such specific functions of their parent companies as research and development and sale or production of certain products.”<sup>171</sup> It goes without saying that such distinction between full-function joint ventures and other joint ventures is quite brief, compared to the well established concept of full-functionality in the EU Commission’s *Jurisdictional Notice*<sup>172</sup>. Moreover, the ‘joint venture provision’ has been deleted in the final published MOFCOM *measures on notification of concentrations*.<sup>173</sup>

As to the notification thresholds, it is considered appropriate that the AML authorises the State Council to establish the notification thresholds and adjust over time according to changing economic situations.<sup>174</sup> Like the EU Merger Regulation<sup>175</sup>, the State Council’s *Provisions on the Standard for Declaration of Concentration of Business Operators*<sup>176</sup> adopts turnover of

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<sup>170</sup> *Interim Measures on the Notification of Business Operators' Concentration* (MOFCOM draft for comments, 20 January 2009), available at <http://fldj.mofcom.gov.cn/aarticle/zcfb/200901/20090106011461.html>, last visited on 29 December 2013, Article 3, translated by Nathan Bush, in ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p134.

<sup>171</sup> *Interim Measures on the Notification of Business Operators' Concentration* (SCLAO draft for comments, 13 March 2009), available at [http://bmyj.chinalaw.gov.cn/lismsPro/law\\_download/fulltext/1236930767681.doc](http://bmyj.chinalaw.gov.cn/lismsPro/law_download/fulltext/1236930767681.doc), last visited on 29 December 2013, Article 3, translated by Nathan Bush, in ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p134.

<sup>172</sup> *Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings*, [2008] OJ C 95/1, part IV.

<sup>173</sup> *Measure for the Undertaking Concentration Declaration* (adopted by the Ministry of Commerce, issued on 21 November 2009 and effective on 1 January 2010). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8183&lib=law&SearchKeyword=Undertaking%20Concentration%20Declaration&SearchCKeyword=>, last visited on 20 December 2013)

<sup>174</sup> AML, *supra* note 9, Article 21. See Zhenguo Wu, ‘Perspectives on the Chinese Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 73, p89.

<sup>175</sup> See *EU Merger Regulation 139/2004*, *supra* note 167, Article 1.

<sup>176</sup> *Provisions of the State Council on the Standard for Declaration of Concentration of Business Operators* (adopted by the State Council of the People’s Republic of China, issued and effective on 3 August 2008). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7024&lib=law&SearchKeyword=Standard%20for%20Declaration>



the undertakings concerned as a proxy to set out alternative notification thresholds. According to the State Council's provisions, the parties to the transaction shall notify the MOFCOM their concentration in cases where "(1) the combined worldwide turnover of all the undertakings concerned in the preceding financial year is more than RMB 10 billion yuan, and the nationwide turnover within China of each of at least two of the undertakings concerned in the preceding financial year is more than RMB 400 million yuan; or (2) the combined nationwide turnover within China of all the undertakings concerned in the preceding financial year is more than RMB 2 billion yuan, and the nationwide turnover within China of each of at least two of the undertakings concerned in the preceding financial year is more than RMB 400 million yuan."<sup>177</sup>

As to the assessment conducted by the merger reviewer, like international prevailing practices such as the relevant provision in the EU Merger Regulation<sup>178</sup>, concentration cases would be reviewed in Phase I or be preceded to an in-depth Phase II investigation depending on the complexity of the particular case.<sup>179</sup> Article 27 of the AML lists factors that merger review authority should take into consideration in its analysis. Most of them are market competition related factors, which are similar to those aspects in the EU and the US.<sup>180</sup> It is noticeable that the effect of the notified transaction on the 'national economic development', as one factor from the perspective of industrial policy rather than competition-related factor, would also be considered by the MOFCOM. In the first blocked *Coca-cola/Huiyuan* transaction the MOFCOM considered six factors in its analysis: the parties' market shares in the relevant market and their controlling power over that market, the degree of market concentration in the relevant market, the impact of the concentration on the market access and technological advancements, the impact of the concentration on the consumers and other undertakings, the impact on competition in the fruit juice beverage market, as well as the impact of the concentration on the 'national economic development'.<sup>181</sup> In the MOFCOM later released

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<sup>177</sup> Ibid, Article 3.

<sup>178</sup> *EU Merger Regulation 139/2004*, *supra* note 167, Article 10.

<sup>179</sup> AML, *supra* note 9, Article 25 and 26.

<sup>180</sup> See Xiaoye Wang and Jessica Su, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar Publishing 2012) 379, p385.

<sup>181</sup> MOFCOM, circular [2009] No.22, available at <http://fldj.mofcom.gov.cn/article/ztzx/200903/20090306108494.shtml> (in Chinese), last visited on 29 December 2013.

official Q&A of *Coca-Cola/Huiyuan* case, the MOFCOM official held that taking the impact of the transaction on national economic development into consideration in merger review is prevailing practice worldwide, which is in line with the AML objectives of protecting the public interest and the socialist market economy.<sup>182</sup> Taking such a non competition-related effect into consideration is argued to demonstrate MOFCOM's readiness to consider industrial policy in merger review.<sup>183</sup> Moreover, it remains unknown as to how this non-competition factor will be balanced by the MOFCOM with other competition related factors.<sup>184</sup>

The AML provides the parties to the transactions with two possible defences to rebut if they can prove either that the pro-competitive impact brought about by the concentration obviously exceeds the anti-competitive impact, or that such concentration meets the public interests.<sup>185</sup> These two defences are based on German competition rules.<sup>186</sup> The notion 'public interests', as demonstrated above, is quite vague in the AML, even though three examples – energy saving, environment protection or disaster relief – have been given in the anticompetitive agreements chapter.<sup>187</sup> In the realm of merger control, reference might be provided by six ministerial agencies' *Provisions on the Takeover of Domestic Enterprises by Foreign Investors (2006)*, which is the main legislation for antitrust review of acquisition of domestic undertakings by foreign investors prior to the AML.<sup>188</sup> According to that rule, the parties to the transaction may

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<sup>182</sup> MOFCOM Spokesman Yao Jian Answering Reporters' Questions regarding Anti-Monopoly Review Decision for Coca-Cola's Acquisition of Huiyuan, available at <http://www.mofcom.gov.cn/article/zhengcejd/bj/200903/20090306124140.shtml>, last visited on 29 December 2013.

<sup>183</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p140.

<sup>184</sup> See Fei Deng, Adrian Emch and Gregory K. Leonard, 'A Hard Landing in the Soft Drink Market – MOFCOM's Veto of the Coca-Cola & Huiyuan Deal', *Global Competition Policy Magazine*, April 2009 Release 2, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1396968](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1396968), last visited on 2 January 2014.

<sup>185</sup> AML, *supra* note 9, Article 28.

<sup>186</sup> See *Act Against Restraints of Competition* in the version published on 15 July 2005 (Bundesgesetzblatt (Federal Law Gazette) I, page 2114; 2009 I page 3850), as last amended by Article 3 of the Act of 26 July 2011 (Federal Law Gazette I, page 1554), § 36(1) and § 42(1), available at [http://shvv.juris.de/englisch\\_gwb/act\\_against\\_restraints\\_of\\_competition.pdf](http://shvv.juris.de/englisch_gwb/act_against_restraints_of_competition.pdf), last visited on 9 December 2013.

<sup>187</sup> See *supra* section 2.1.3 Multiple and (potentially) conflicting objectives at pp.7-8.

<sup>188</sup> *Provisions on the Takeover of Domestic Enterprises by Foreign Investors* (No. 10 [2006], promulgated by the Ministry of Commerce, State Assets Supervision and Administration Commission of the State Council, State Administration of Taxation, State Administration for Industry and Commerce, China Securities Regulatory Commission and State Administration of Foreign Exchange on 8 August 2006 and effective since 8 September 2006), translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=5420&lib=law&SearchKeyword=&SearchCKeyword=%CD%E2%B9%FA%CD%B6%D7%CA%D5%DF%B2%A2%B9%BA>, last visited on 9 December. Chapter V

apply for exemption in cases where “(1)[t]he takeover may improve the conditions for fair competition in the market; (2) A loss-making enterprise is taken over and the employment is ensured; (3) The takeover helps the absorption of advanced technologies and management personnel and is able to improve the enterprise's international competitiveness; or (4) The takeover may improve the environment.”<sup>189</sup> One Chinese leading scholar held that the public interests defence could be applied in the last three situations.<sup>190</sup> However, this interpretation of ‘public interests’ has not been reflected in the AML. In the absence of a well-defined scope for the public interests defence, as an antimonopoly law practitioner noted, concentrations with obviously anti-competitive impact could escape from the balancing test in the name of ‘public interests’ and “eviscerate the rule”, *inter alia* in the SOE-involved cases.<sup>191</sup>

In the cases of domestic undertakings acquired by foreign investors, notified concentrations might be required to undergo an additional ‘national security review’ if the transaction concerned involves national security-related industries.<sup>192</sup> While in merger cases the EU leaves jurisdiction over national security-related issues to the Member States,<sup>193</sup> this additional review is similar with the US practice of examining foreign investment by the Committee on Foreign Investment in the United States (‘CFIUS’).<sup>194</sup> Vice Chairman of the National People’s Congress Xu Jialu, in commenting on the AML draft, held that the concept ‘national security’ should include national defence security, information security, environmental security, and economic security.<sup>195</sup> To establish a review system for national security purpose, the State

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“Anti-monopoly Review” has been deleted by the Decision of the Ministry of Commerce on Amending the Provisions on the Takeover of Domestic Enterprises by Foreign Investors (No.6 [2009], issued by the Ministry of Commerce on 22 June 2009), translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7673&lib=law&SearchKeyword=&SearchCKeyword=%CD%E2%B9%FA%CD%B6%D7%CA%D5%DF%B2%A2%B9%BA>, last visited on 9 December 2013.

<sup>189</sup> Ibid, Article 54.

<sup>190</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p614.

<sup>191</sup> Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p137.

<sup>192</sup> AML, *supra* note 9, Article 31.

<sup>193</sup> See *Consolidated Version of the Treaty on the Functioning of the European Union* [2012] OJ C 326/47, Article 346.

<sup>194</sup> See Zhenguo Wu, ‘Perspectives on the Chinese Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 73, p101; Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p116; Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p91; Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed) *Report on Competition Law and Policy of China 2012* (Law Press, China, 2013), p199.

<sup>195</sup> Jialu Xu, ‘Enhancing Supervision of Mergers and Acquisitions, Preventing Abuse of Administrative Power to

Council and the MOFCOM have laid down several substantial and procedural rules.<sup>196</sup> According to the State Council's Notice, the security review should be conducted in following cases: "foreign investors' mergers and acquisitions of domestic military industrial enterprises and supportive military industrial enterprises, enterprises surrounding major and sensitive military facilities, and other entities relating to the national defense security; foreign investors' mergers and acquisitions of domestic enterprises relating to important agricultural products, important energies and resources, important infrastructural facilities, important transportation services, key technologies, manufacturing of major equipment, etc., which relate to the national security, and whose actual controlling power may be obtained by foreign investors."<sup>197</sup> It seems the broad interpretation of the term 'national security', either unofficially by the lawmaking official or officially by the Chinese government, relates more to industrial policy interests in fundamental sectors, rather than merely the national military or security issue.<sup>198</sup> More importantly, it has been argued that the AML diverges from US practice by incorporating national security consideration into competition law, while the US uses separate investment statutes to address national security issue.<sup>199</sup> As overseas investments by Chinese enterprises increase rapidly, some observers believe that without proper limitation application of this additional national security review will discourage foreign investment.<sup>200</sup> So far, in practice it

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Exclude and Restrict Competition', available at <http://china.findlaw.cn/jingjifa/fldf/lyjz/03137995.html> (in Chinese), last visited on 29 December 2013.

<sup>196</sup> *Notice of the General Office of the State Council on the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (No.6 [2011] of the General Office of the State Council, issued and effective on 3 March 2011), translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8516&lib=law&SearchKeyword=&SearchCKeyword=%CD%E2%B9%FA%CD%B6%D7%CA%D5%DF%B2%A2%B9%BA>, last visited on 9 December 2013. *Provisions of the Ministry of Commerce on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (No.53 [2011], Announcement of the Ministry of Commerce, issued on 25 August 2011 and effective since 1 September 2011), translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8919&lib=law&SearchKeyword=&SearchCKeyword=%CD%E2%B9%FA%CD%B6%D7%CA%D5%DF%B2%A2%B9%BA>, last visited on 9 December 2013.

<sup>197</sup> *Notice of the General Office of the State Council on the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, *supra* note 196, Article 1(1).

<sup>198</sup> See Yong Huang, 'Pursing the Second Best: The History, Momentum, and Remaining Issues of China's Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 117, p129; Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p92; Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p116.

<sup>199</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p92.

<sup>200</sup> See Jessica Su and Michael Han, 'China's Antimonopoly Law: Status Quo and Outlook' (2008) 8(1) *Competition Policy International*, available at

remains unknown whether there has been any notified transaction that was reviewed under this provision.<sup>201</sup>

### 3. The enforcement of the AML

#### 3.1 The enforcement regime

Due to China's civil law tradition, the enforcement regime of the AML is more influenced by the EU administrative agency-oriented model.<sup>202</sup> This is different with the US antitrust law where court-oriented model is the main feature.<sup>203</sup> Although currently more attention has been paid to the private enforcement of competition law in both of the EU<sup>204</sup> and China<sup>205</sup>, it has been admitted in both jurisdictions that public enforcement still plays the main role in implementing competition rules.<sup>206</sup>

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<https://www.competitionpolicyinternational.com/chinas-antimonopoly-law-status-quo-and-outlook/>, last visited on 2 January 2014.

<sup>201</sup> See Xiaoye Wang and Jessica Su, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar 2012) 379, p386.

<sup>202</sup> See e.g. Xianchu Zhang, 'An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy' (2009) 43 *The International Lawyer* 1469, p1489; Youngjin Jung and Qian Hao, 'The New Economic Constitution in China: A Third Way for Competition Regime' (2003) 24(1) *Northwestern Journal of International Law & Business* 107, pp.124-125.

<sup>203</sup> See Xianchu Zhang, 'An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy' (2009) 43 *The International Lawyer* 1469, p1489; Eva Choi, 'Seeking Stones in the Red River: The Inevitable Evolution of China's Anti Monopoly Law' (2010) 7(1) *Journal of Law, Economics & Policy* 163, pp.168-170.

<sup>204</sup> On 11 June 2013 the EU Commission adopted a proposal for a Directive on damages actions for breaches of EU competition law. The proposal is submitted to the EU Council and the EU Parliament under the legislative procedure. In addition, the Commission issued a *Recommendation on common principles for injunctive and compensatory collective redress mechanisms in the Member States concerning violations of rights granted under EU law*, and adopted a *Communication on quantifying harm in antitrust damages actions*.

<sup>205</sup> The Chinese Supreme Court in 2012 issued its first judicial interpretation *Provisions of the Supreme People's Court on Several Issues concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct*, which came into force on 1 June 2012, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=9300&lib=law&SearchKeyword=Application%20of%20Law%20in%20the%20Trial%20of%20Civil%20Dispute%20Cases&SearchCKeyword=>, last visited on 29 October 2013.

<sup>206</sup> For this viewpoint in EU see e.g. Joaquín Almunia, Vice President of the EU Commission responsible for Competition Policy, 'Antitrust Damages in EU Law and Policy', speech delivered at *College of Europe GCLC Annual Conference* on 7 November 2013, available at [http://europa.eu/rapid/press-release\\_SPEECH-13-887\\_en.htm](http://europa.eu/rapid/press-release_SPEECH-13-887_en.htm), last visited on 29 January 2014; on the part of China, this viewpoint has been supported by, e.g., Qiong Zhang, chairman of the expert consultation panel of the Anti-monopoly Committee of the State Council, opening speech delivered at *2012 China Anti-monopoly Private Enforcement Forum* on 17 April 2012, his view is quoted by Yong Huang and Yunyu Shen, 'The Latest

Prior to the enactment of the AML, the Ministry of Commerce ('MOFCOM')<sup>207</sup>, National Development and Reform Commission ('NDRC')<sup>208</sup> and State Administration for Industry and Commerce ('SAIC')<sup>209</sup>, as well as their subordinate agencies at the provincial level, have already begun to deal with competition issues, each responsible for certain aspects. Absent a comprehensive competition law, the enforcement powers of these administrative authorities were sourced from different laws and regulations. The MOFCOM, the major regulator for mergers and acquisitions, was authorised by the *Interim Provisions on the Takeover of Domestic Enterprises by Foreign Investors*<sup>210</sup>. The SAIC was empowered by the *Anti-Unfair Competition Law*<sup>211</sup> and has accumulated much experience in dealing with most unfair competition behaviour as well as certain monopolistic behaviour. The NDRC was endowed

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Developments of Chinese Anti-Monopoly Law and Policy Making and Cooperation', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed) *Report on Competition Law and Policy of China 2012* (Law Press, China, 2013) 32, p38.

<sup>207</sup> The MOFCOM was formed in the 2003 central government reorganization. The MOFCOM is the competent authority of ministerial level directly under the State Council in charge of formulating policy on foreign trade, export and import regulations, foreign direct investments, consumer protection, market competition and negotiating bilateral and multilateral trade agreements. More detailed functions of the MOFCOM could see its official website <http://english.mofcom.gov.cn/column/mission2010.shtml>, last visited on 20 January 2014.

<sup>208</sup> The NDRC is a powerful macroeconomic planning body with broad authority over nationwide industrial policy and economic policy. More detailed functions of the NDRC could see its official website <http://en.ndrc.gov.cn/mfndrc/default.htm>, last visited on 20 January 2014.

<sup>209</sup> The SAIC is the competent authority of ministerial level directly under the State Council in charge of market supervision/regulation and related law enforcement through administrative means. With creating a regulated and harmonized market environment of fairness, justice and faithfulness for the coordinated socioeconomic development as its objective, the SAIC functions in maintaining market order and protecting the legitimate rights and interests of businesses and consumers by carrying out regulations in the fields of enterprise registration, competition, consumer protection, trademark protection and combating economic illegalities. The SAIC also coordinates local Administrations for Industry and Commerce at/below provincial level, and gives relevant guidance thereof. More detailed functions of the SAIC could see its official website <http://www.saic.gov.cn/english/index.html>, last visited on 20 January 2014.

<sup>210</sup> *Interim Provisions on the Takeover of Domestic Enterprises by Foreign Investors* (jointly adopted by the Ministry of Commerce, State Assets Supervision and Administration Commission of the State Council, State Administration of Taxation, State Administration for Industry and Commerce, China Securities Regulatory Commission and State Administration of Foreign Exchange on 8 August 2006 and effective since 8 September 2006, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=5420&lib=law&SearchKeyword=Interim%20Provisions%20on%20the%20Takeover%20of%20Domestic%20Enterprises&SearchCKeyword=>, amended in 2009, last visited on 20 January 2014), Article 51.

<sup>211</sup> AUCL, *supra* note 9, Article 3.



by the *Price law*<sup>212</sup> and *Interim Provisions on Preventing the Acts of Price Monopoly*<sup>213</sup> with enforcement power to prevent and cease price-related monopolistic behaviour.

The AML has established a two-layer, three-pronged enforcement regime within the Chinese administrative structure. Under the State Council, a new Anti-Monopoly Committee has been created to organise, coordinate and guide the enforcement of the AML.<sup>214</sup> The Anti-Monopoly Committee is composed of the principals of relevant ministries and committees of the State Council.<sup>215</sup> It has released the first guideline in the Chinese competition law system – *Guide for the Definition of the Relevant Market*.<sup>216</sup>

Prior to the adoption of the AML, different state authorities, especially the MOFCOM and the SAIC, claimed competence over anti-monopoly related matters.<sup>217</sup> To facilitate the enactment of the AML and to compromise the power struggle, the AML merely states that the AML enforcement authority/authorities designated by the State Council shall be responsible for the AML enforcement work, without explicitly providing which state agency or agencies have the jurisdiction.<sup>218</sup> Mr. Cao Kangtai, Director of the Legislative Affairs Office of the State Council, when submitting the AML draft to the Standing Committee of 10th National People's Congress

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<sup>212</sup> *Price Law of the People's Republic of China* (issued by Standing Committee of the National People's Congress on 29 December 1997, effective since 1 May 1998, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=76&lib=law&SearchKeyword=price%20law&SearchCKeyword=>, last visited on 20 January 2014), Article 5.

<sup>213</sup> *Interim Provisions on Preventing the Acts of Price Monopoly* (issued by the NDRC on 18 June 2003 and effective since 1 November 2003, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=2936&lib=law&SearchKeyword=Interim%20Provisions%20on%20Preventing&SearchCKeyword=>, last visited on 20 January 2014, now has been replaced by the *Provisions against Price Fixing*, *infra* note 232), Article 10.

<sup>214</sup> AML, *supra* note 9, Article 9.

<sup>215</sup> See *Notice of the General Office of the State Council on the Main Functions and Members of the Anti-Monopoly Commission of the State Council* (issued by the General Office of the State Council, effective on 28 July 2008, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7190&lib=law&SearchKeyword=&SearchCKeyword=%B9%FA%CE%F1%D4%BA%B7%B4%C2%A2%B6%CF%CE%AF%D4%B1%BB%E1>, last visited on 20 January 2014).

<sup>216</sup> *Guide of the Anti-Monopoly Committee of the State Council for the Definition of the Relevant Market* (issued and effective on 24 May 2009). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7575&lib=law&SearchKeyword=Definition%20of%20the%20Relevant%20Market&SearchCKeyword=>, last visited on 20 January 2014)

<sup>217</sup> See Xianchu Zhang, 'An Anti-Monopoly Legal Regime in the Making in China as a Socialist Market Economy' (2009) 43 *The International Lawyer* 1469, pp.1478-1479; Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p99.

<sup>218</sup> AML, *supra* note 9, Article 10.

in June 2006, stated that:

“[T]here exist[s] consensus among interested parties that, regarding the design of the anti-monopoly enforcement structure, current structure should be maintained in order to ensure anti-monopoly law enforcement. On the other hand, the design should be forward-looking and should leave space for future agency reform and restructuring. It is suggested that the anti-monopoly law only stipulates the enforcement authority’s responsibilities and working procedure, but leaves the question of which agency(ies) will be empowered to enforce the law to the State Council to stipulate separately.”<sup>219</sup>

To date the specific enforcement work of the AML is still undertaken and shared by the MOFCOM, the NDRC and the SAIC.<sup>220</sup> The division of the enforcement power of the AML by three administrative authorities remains almost the same as that under the old regime prior to the enactment of the AML. Based on the fundamental principles and rules created by the AML, implementing rules and guidelines have gradually been laid down by competent authorities within their respective discretion in order to establish a complete and workable competition law legislative system. The MOFCOM’s main responsibility is to review merger cases. A new Anti-Monopoly Bureau was formed within the MOFCOM to implement the AML.<sup>221</sup> In addition, the Anti-Monopoly Bureau also undertakes the day-to-day work of the

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<sup>219</sup> See Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p588. Mr. Cao Kangtai’s statement regarding the AML draft available at [http://www.npc.gov.cn/wxzl/gongbao/2007-10/09/content\\_5374671.htm](http://www.npc.gov.cn/wxzl/gongbao/2007-10/09/content_5374671.htm) (in Chinese), last visited on 4 December 2013.

<sup>220</sup> For more detailed information about the enforcement authorities (MOFCOM, NDRC and SAIC) in implementing the AML, could see Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, pp.99-104.

<sup>221</sup> There are six divisions in the Anti-Monopoly Bureau: the General Affairs Division, Competition Policy Division, Investigation Division I, Investigation Division II, Supervision and Law Enforcement Division, and Economic Analysis Division. Ming Shang, Director General of the Anti-Monopoly Bureau, introduced the function of each division in the interview conducted by Antitrust Source in February 2009: “The General Affairs Division is responsible for administrative affairs of the Bureau and external liaison. The Competition Policy Division is responsible for drafting relevant regulations on the concentrations of undertakings and formulating relevant rules and regulatory documents. Investigation Division I and Investigation Division II are responsible for antimonopoly review of filings of concentrations of undertakings. The Supervision and Law Enforcement Division mainly is responsible for handling and investigating reported concentrations of undertakings, and punishing non-compliance with the law. The Economic Analysis Division is responsible for conducting economic analysis on concentrations of undertakings in the process of antimonopoly review.” Available at [http://www.americanbar.org/content/dam/aba/publishing/antitrust\\_source/Feb09\\_ShangIntrvw2\\_26f.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Feb09_ShangIntrvw2_26f.authcheckdam.pdf), last visited on 20 January 2014, at 2.



Anti-Monopoly Committee.<sup>222</sup> In the realm of merger review, a number of substantial and procedural rules have been adopted by the MOFCOM, including *Measure for the Undertaking Concentration Declaration*<sup>223</sup>, *Measure for the Undertaking Concentration Examination*<sup>224</sup>, *Interim Provisions on the Divestiture of Assets or Business in the Concentration of Business Operators*<sup>225</sup>, *Interim Provisions on Assessing the Impact of Concentration of Business Operators on Competition*<sup>226</sup>, *Interim Measures for Investigating and Handling Failure to Legally Declare the Concentration of Business Operators*<sup>227</sup>, *Interim provisions on the Standards Applicable to Simple Cases of Concentrations of Undertakings*<sup>228</sup>. Currently the MOFCOM has published draft *Provisions for the Imposition of*

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<sup>222</sup> Interview with Ming Shang, Director General of the Anti-Monopoly Bureau under the Ministry of Commerce of the People's Republic of China, February 2009, available at [http://www.americanbar.org/content/dam/aba/publishing/antitrust\\_source/Feb09\\_ShangIntrvw2\\_26f.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Feb09_ShangIntrvw2_26f.authcheckdam.pdf), last visited on 20 January 2014, at 3.

<sup>223</sup> *Measure for the Undertaking Concentration Declaration* (adopted by the Ministry of Commerce, issued on 21 November 2009 and effective on 1 January 2010). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8183&lib=law&SearchKeyword=Undertaking%20Concentration%20Declaration&SearchCKeyword=>, last visited on 20 January 2014)

<sup>224</sup> *Measure for the Undertaking Concentration Examination* (adopted by the Ministry of Commerce, issued on 24 November 2009 and effective on 1 January 2010). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8184&lib=law&SearchKeyword=Undertaking%20Concentration%20Examination&SearchCKeyword=>, last visited on 20 January 2014)

<sup>225</sup> *Interim Provisions on the Divestiture of Assets or Business in the Concentration of Business Operators* (adopted by the MOFCOM, issued and effective on 5 July 2010). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8191&lib=law&SearchKeyword=Interim%20Provisions%20on%20the%20Divestiture%20of%20Assets&SearchCKeyword=>, last visited on 20 January 2014). This Interim Provisions will be replaced by the *Provisions for the Imposition of Restrictive Conditions on Concentrations of Business Operators*, the draft of which was published on 28 March 2013 by the MOFCOM and followed by a public consultation period (concluded on 26 April 2013).

<sup>226</sup> *Interim Provisions on Assessing the Impact of Concentration of Business Operators on Competition* (adopted by the MOFCOM, issued on 29 August 2011 and effective on 5 September 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8929&lib=law&SearchKeyword=Assessing%20the%20Impact%20of%20Concentration%20of%20Business%20Operators&SearchCKeyword=>, last visited on 20 January 2014)

<sup>227</sup> *Interim Measures for Investigating and Handling Failure to Legally Declare the Concentration of Business Operators* (adopted by the MOFCOM, issued on 30 December 2011 and effective on 1 February 2012). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=9151&lib=law&SearchKeyword=Investigating%20and%20Handling%20Failure%20to%20Legally%20Declare&SearchCKeyword=>, last visited on 20 January 2014)

<sup>228</sup> *Interim Provisions on the Standards Applicable to Simple Cases of Concentrations of Undertakings* (adopted by the MOFCOM, issued on 11 February 2014 and effective since 12 February 2014, translation available by subscription at

*Restrictive Conditions on Concentrations of Business Operators*<sup>229</sup> for public comments. As already mentioned above in the ‘concentration section’,<sup>230</sup> in the realm of merger review the State Council issued its *Provisions on the Standard for Declaration of Concentration of Business Operators*<sup>231</sup> as soon as the AML came into force.

The NDRC is responsible for addressing price-related anticompetitive agreements and abusive behaviour. This role is essentially assumed by the Price Supervision and Anti-Monopoly Bureau. Within its discretion, the NDRC has adopted two price-related implementing rules, *Provisions against Price Fixing*<sup>232</sup> and *Provisions on the Administrative Procedures for Law Enforcement against Price Fixing*<sup>233</sup>.

The SAIC, another anti-monopoly enforcement authority for non-merger issues, is responsible for enforcing rules against non price-related anticompetitive agreements and abusive behaviour. Anti-Monopoly and Anti-Unfair Competition Enforcement Bureau was formed to implement the law. Like the other two enforcement authorities, a number of implementing rules – substantial or procedural – have been laid down, including the *Provisions on the Prohibition of Abuse of Dominant Market Position*<sup>234</sup>, the *Provisions on the Prohibition of Monopolistic*

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<http://www.lawinfochina.com/display.aspx?id=16311&lib=law&SearchKeyword=&SearchCKeyword=%be%ad%d3%aa%d5%df%bc%af%d6%d0%bc%f2%d2%d7%b0%b8%bc%fe>, last visited on 20 October 2014)

<sup>229</sup> *Provisions for the Imposition of Restrictive Conditions on Concentrations of Business Operators* (draft for comments, published on 28 March 2013 by the MOFCOM, if adopted this provision will replace the *Interim Provisions on the Divestiture of Assets or Business in the Concentration of Business Operators* as indicated in *supra* note 225), available at <http://tfs.mofcom.gov.cn/article/as/201303/20130300068492.shtml> (in Chinese), last visited on 20 January 2014.

<sup>230</sup> See *supra* section 2.2.3 Concentration.

<sup>231</sup> *Provisions of the State Council on the Standard for Declaration of Concentration of Business Operators* (adopted by the State Council of the People’s Republic of China, issued and effective on 3 August 2008). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7024&lib=law&SearchKeyword=Standard%20for%20Declaration%20of%20Concentration%20of%20Business%20Operators&SearchCKeyword=>, last visited on 20 January 2014)

<sup>232</sup> *Provisions against Price Fixing* (adopted by the NDRC, issued on 29 December 2010 and effective since 1 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8440&lib=law&SearchKeyword=Provisions%20against%20Price%20Fixing&SearchCKeyword=>, last visited on 20 January 2014)

<sup>233</sup> *Provisions on the Administrative Procedures for Law Enforcement against Price Fixing* (adopted by the NDRC, issued on 29 December 2010 and effective since 1 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8439&lib=law&SearchKeyword=Administrative%20Procedures%20for%20Law%20Enforcement%20against%20Price%20Fixing&SearchCKeyword=>, last visited on 20 January 2014)

<sup>234</sup> *Provisions for the Industry and Commerce Administrations on the Prohibition of Abuse of Dominant Position*

*Agreements*<sup>235</sup>, *the Provisions on the Procedures for the Administrative Departments for Industry and Commerce to Investigate and Handle Cases of Monopolization Agreements and Abuse of Dominant Market Position*<sup>236</sup>, *the Provisions for the Industry and Commerce Administrations to Stop Acts of Abusing Administrative Power for the Purpose of Eliminating or Limiting Competition*<sup>237</sup>, *the Provisions on the Procedure for the Industry and Commerce Administrations to Stop Acts of Abusing Administrative Power for Excluding or Limiting Competition*<sup>238</sup>.

In case that the undertakings are dissatisfied with an administrative decision delivered by one of the enforcement authorities, Article 53 of the AML provides them with the right to appeal and distinguishes the procedures between the merger cases and non-merger cases. For the decisions related to merger control review, administrative reconsideration of the original decision by a higher administrative authority is a prerequisite prior to parties to the transaction lodging an application for judicial review. For the decisions related to anticompetitive agreements and abusive behaviour, the undertakings concerned have two possible courses of action. They may

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(adopted by the SAIC, issued on 31 December 2010 and effective since 1 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8540&lib=law&SearchKeyword=Prohibition%20of%20Abuse%20of%20Dominant%20Market%20Position&SearchCKeyword=>, last visited on 20 January 2014)

<sup>235</sup> *Provisions for the Industry and Commerce Administrations on the Prohibition of Monopolistic Agreements* (adopted by the SAIC, issued on 31 December 2010 and effective since 1 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8539&lib=law&SearchKeyword=Prohibition%20of%20Monopolistic%20Agreements&SearchCKeyword=>, last visited on 20 January 2014)

<sup>236</sup> *Provisions on the Procedures for the Administrative Departments for Industry and Commerce to Investigate and Handle Cases of Monopolization Agreements and Abuse of Dominant Market Position* (adopted by the SAIC, issued on 26 May 2009 and effective since 1 July 2009). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7706&lib=law&SearchKeyword=Procedures%20for%20the%20Administrative%20Departments%20for%20Industry%20and%20Commerce%20to%20Investigate%20and%20Handle&SearchCKeyword=>, last visited on 20 January 2014)

<sup>237</sup> *Provisions for the Industry and Commerce Administrations to stop Acts of Abusing Administrative Power for the Purpose of Eliminating or Limiting Competition* (adopted by the SAIC, issued on 31 December 2010 and effective since 1 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8538&lib=law&SearchKeyword=Stop%20Acts%20of%20Abusing%20Administrative%20Power%20for%20the%20Purpose&SearchCKeyword=>, last visited on 20 January 2014)

<sup>238</sup> *Provisions on the Procedure for the Industry and Commerce Administrations to Stop Acts of Abusing Administrative Power for Excluding or Limiting Competition* (adopted by the SAIC, issued on 26 May 2009 and effective since 1 July 2009). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7570&lib=law&SearchKeyword=to%20Stop%20Acts&SearchCKeyword=>, last visited on 20 January 2014)

either request reconsideration by a higher administrative authority, or apply for judicial review of the original decision.<sup>239</sup> Firstly, the chance for the undertakings to win an appeal case in the procedure of administrative reconsideration is limited.<sup>240</sup> Given the fact that most public enforcement decisions are delivered by the MOFCOM, the NDRC or the SAIC rather than their subordinate authorities at the provincial level, in most cases dissatisfied undertakings could only, in the administrative procedure, appeal to the same administrative authority, because the *Administrative Reconsideration Law*<sup>241</sup> provides that administrative decisions issued by the ministries under the State Council is to be reviewed by the same authority that made the original decision.<sup>242</sup> Thus, it is quite doubtful whether the reconsideration of the original decision, even conducted by another division other than the original decision-making division, would re-analyze the case and overthrow the original decision. Secondly, the requirement of administrative reconsideration as a precondition for judicial review in merger cases, which distinguishes merger cases and non-merger cases, has been criticized to be not well grounded.<sup>243</sup> The reason for such arrangement could be that, as the MOFCOM officials claimed, merger cases are more complicated and require more economic-related analysis.<sup>244</sup> Even it is true to some extent, a compulsory administrative reconsideration would take much time before advancing to the judicial review process.<sup>245</sup> Moreover, compared to the administrative reconsideration, judicial review is argued to be a more impartial referee.<sup>246</sup> From another perspective, such procedural difference between merger cases and non-merger

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<sup>239</sup> AML, *supra* note 9, Article 53.

<sup>240</sup> See Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p266.

<sup>241</sup> *Administrative Reconsideration Law of the People's Republic of China* (adopted at the Ninth Session of the Standing Committee of the Ninth National People's Congress on 29 April 1999, effective since 1 October 1999 and amended in 2009, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=5279&lib=law&SearchKeyword=&SearchCKeyword=%D0%D0%D5%FE%B8%B4%D2%E9%B7%A8>, last visited on 20 January 2014).

<sup>242</sup> *Ibid*, Article 14.

<sup>243</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, pp.637-639.

<sup>244</sup> See Zhenguo Wu, 'Perspectives on the Chinese Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 73, pp.113-114. See also Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p111.

<sup>245</sup> In fact, according to published competition authorities' decisions and court judgments in China, it cannot be concluded that merger cases are more complicated, or less complicated than non-merger cases. Some antimonopoly civil cases before Chinese courts, such as the *Qihoo vs. Tencent* abuse of dominance case as introduced below, are quite complicated and require extensive economic analysis.

<sup>246</sup> See Xiaoye Wang, 'The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress' (2009) 54 *The Antitrust Bulletin* 579, p592.

cases is untenable since there has been no solid evidence demonstrating that Chinese courts are better suited to review other non-merger rulings.<sup>247</sup>

Judges of Chinese courts could deliver their opinions, either in the judicial review of administrative decisions, or in antimonopoly civil lawsuits. Article 50 of the AML provides the legal basis for private parties to lodge civil anti-monopoly cases to the competent courts.<sup>248</sup> The Supreme Court in April 2008 enacted its *Provisions on the Cause of Action of Civil Cases*<sup>249</sup>, granting the jurisdiction over anti-monopoly cases to the IP tribunals of competent Chinese courts.<sup>250</sup> Later in July 2008, the Supreme Court distributed the *Circular on Carefully Studying and Implementing the Anti-Monopoly Law*<sup>251</sup> within the Chinese court system, reiterating IP tribunals' jurisdiction over IP-related anti-monopoly cases and other anti-monopoly cases. Such arrangement bases on the well-perceived fact that judges in the IP tribunals are more experienced and particularly sensitive to the unique features of IPR when approaching IPR-related anti-monopoly cases.<sup>252</sup> The Supreme Court in May 2012 released the *Provisions on Several Issues concerning the Application of Law in the Trial of Civil Dispute*

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<sup>247</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p111.

<sup>248</sup> Article 50 of the AML, *supra* note 9, reads as "The business operators that carry out the monopolistic conducts and cause damages to others shall bear the civil liability according to law."

<sup>249</sup> *Provisions on the Cause of Action of Civil Cases* (Adopted and issued by the Chinese Supreme Court on 4 February 2008, amended on 18 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8607&lib=law&SearchKeyword=&SearchCKeyword=%C3%F1%CA%C2%B0%B8%BC%FE%B0%B8%D3%C9%B9%E6%B6%A8>, last visited on 20 January 2014)

<sup>250</sup> Since 1994, the Chinese Supreme Court has permitted to establish IPR tribunals within competent Chinese courts, see *Circular of the Supreme People's Court on Further Strengthening the Judicial Protection of Intellectual Property Rights* (No. 111 [1994] of the Supreme People's Court, issued on 29 September 1994), available by subscription at <http://vip.chinalawinfo.com/newlaw2002/slc/slc.asp?db=chl&gid=10608> (in Chinese, last visited on 3 December 2013). In fact, before the release of that circular, the Beijing Intermediate and High Courts, as the first two courts in the country, established IPR tribunals in august 1993. In October 1996, the Supreme Court set up its IPR tribunal. See the Supreme Court's *Intellectual Property Protection by Chinese Courts in 2009* (White Paper 2009), English version available at [http://www.court.gov.cn/zscq/bhcg/201004/t20100426\\_4545.html](http://www.court.gov.cn/zscq/bhcg/201004/t20100426_4545.html), last visited on 3 December 2013. By the end of 2012, 420 IPR tribunals have been established in China. See the Supreme Court's *Intellectual Property Protection by Chinese Courts in 2012* (White Paper 2012), English version available at [http://www.court.gov.cn/zscq/bhcg/201304/t20130426\\_183662.html](http://www.court.gov.cn/zscq/bhcg/201304/t20130426_183662.html), last visited on 3 December 2013.

<sup>251</sup> *The Circular on Carefully Studying and Implementing the Anti-Monopoly Law* (issued by the Supreme Court on 28 July 2008, available at <http://vip.chinalawinfo.com/newlaw2002/slc/slc.asp?db=chl&gid=107282> (in Chinese), last visited on 20 January 2014.)

<sup>252</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p109.

*Cases Arising from Monopolistic Conduct* ('AML Judicial Interpretation')<sup>253</sup>. This first ever AML Judicial Interpretation clarifies the relationship of anti-monopoly administrative investigations and the judicial process, the jurisdiction of competent courts, allocation of burden of proof, expert witness and independent professional institutions and so forth.

It is interesting to notice that, without sufficient experience in the early years in implementing the AML, Chinese administrative enforcement authorities and the courts in practice demonstrated their willingness to draw successful experiences from the prevailing international practice. For instance, in the blocked *Coca-Cola/Huiyuan* merger case, the MOFCOM adopted the concept 'leverage effect' to reject the merger application.<sup>254</sup> It is believed that the reason is similar to the rationales employed by the Australian Competition and Consumer Commission's *Coca-Cola Amatil/Berri* case<sup>255</sup> and EU *GE/Honeywell* case<sup>256 257</sup>.

In the private enforcement of the AML, one Chinese court in the judgment of a significant civil anti-monopoly lawsuit also quoted some observations made by the European Commission on the Instant Messaging market in *Microsoft/Skype*<sup>258</sup> merger case. *Qihoo vs. Tencent* is the most

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<sup>253</sup> *Provisions of the Supreme People's Court on Several Issues concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct* (Interpretation No.5 [2012] of the Supreme People's Court, effective since 1 June 2012). Supreme Court's judicial interpretations in practice are legally binding on the courts in China. (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=9300&lib=law&SearchKeyword=Application%20of%20Law%20in%20the%20Trial%20of%20Civil%20Dispute%20Cases&SearchCKeyword=>, last visited on 20 January 2014) ('AML judicial interpretation')

<sup>254</sup> See MOFCOM, circular [2009] No.22, available at <http://fdj.mofcom.gov.cn/article/ztxx/200903/20090306108494.shtml> (in Chinese), last visited on 29 December 2013.

<sup>255</sup> ACCA assessment of Coca-Cola Amatil Limited's proposed acquisition of Berri Limited, available at <http://transition.accc.gov.au/content/item.phtml?itemId=503214&nodeId=933cf0f7f72fc1bbe102c39b6243b815&f=n=Coca-Cola+Amatil+Ltd's+proposed+acquisition+of+Berri+Ltd+-+8+October+2003+-+re+carbonated+soft+drink+and+fruit+juice.pdf>, last visited on 20 January 2014.

<sup>256</sup> Case COMP/M.2220, *General Electric / Honeywell*, Commission Decision of 3 July 2001, [2004] OJ L 48/1.

<sup>257</sup> See Wentong Zheng, 'China's New Merger Review Regime under the Antimonopoly Law: A Protectionist Tool?' (2010) 22(1) *Michigan International Lawyer* 3, pp.4-5; Deborah Healey, 'China's Anti-Monopoly Law: Agent of Competition Enhancement or Engine of Industrial Policy? Comment on Wang and Su' in Daniel Zimmer (ed) *The Goals of Competition Law* (Edward Elgar 2012) 398, pp.405-406.

<sup>258</sup> COMP/M.6281 – *Microsoft/Skype*, Commission decision pursuant to Article 6(1) (b) of Council Regulation No 139/2004, full text is available at [http://ec.europa.eu/competition/mergers/cases/decisions/m6281\\_20111007\\_20310\\_2079398\\_EN.pdf](http://ec.europa.eu/competition/mergers/cases/decisions/m6281_20111007_20310_2079398_EN.pdf). The General Court on 11 December 2013 dismissed Cisco System's appeal of the Commission decision of October 2011 to clear the acquisition of Skype by Microsoft (T-79/12, ECLI:EU:T:2013:635, not yet reported).



high-profile and complicated anti-monopoly lawsuit in the software industry before the Chinese court since the enactment of the AML in 2008. Qihoo, the plaintiff, complained to the High Court of Guangdong Province ('the Guangdong Court'), alleging that Tencent infringed the AML by firstly leveraging its dominant position from the market for instant messaging software products ('IM market') onto the market for internet security software products ('security software market') by forcing its users to un-install the plaintiff's products and secondly abusively tying two of its software products. The unique pricing and profit mode in the IM market – the basic IM services are free of charge – gives rise to the difficulty in determining the scope of the relevant market since the SSNIP test might not work as an effective tool to find the substitutes. On 28 March 2013, the Guangdong Court issued its judgment, finding that Qihoo wrongly defined the scope of relevant product and geographic market, and Tencent did not possess a dominant position in the IM market.<sup>259</sup>

It is the *first* anti-monopoly case where some observations made by the EU Commission in an EU competition case have been used by the parties to support their viewpoints, and then been confirmed and quoted by a Chinese court in its judgment. The Guangdong Court quoted the reason put forward by the applicants in EU *Microsoft/Skype* case that, from the perspective of consumers, IM services "are increasingly used as an adjunct to other activities", and "a user experience which integrates a range of communication functionalities", such as Facebook and Google+, has been increasingly demanded.<sup>260</sup> Similarly as what has been observed by the EU Commission in the *Microsoft/Skype* merger case, the Guangdong Court considered that QQ was not a "must have" product.<sup>261</sup> The Guangdong Court held that it has been increasingly common that the consumers (could) have highly overlapped social networks on several IM platforms and they could thus freely and immediately switch to other alternatives.<sup>262</sup> The Guangdong Court maintained that consumers would switch to other free alternatives once the successful software provider started to charge for the basic services, because consumers prefer undertaking the

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<sup>259</sup> The full text of the judgment (in Chinese) could be accessed on the website of the Guangdong Court, <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130328040159946185> (last visited on 29 October 2013, hereinafter 'the Guangdong Court judgment'). On 11 April 2013, Qihoo appealed to the Chinese Supreme Court against the first instance judgment of the Guangdong Court. The Supreme Court held a public hearing on 26 and 27 Nov 2013, and on 16 October 2014 delivered the final judgment, in which the Supreme Court upheld the first instance decision and most viewpoints of the Guangdong Court, the full text of the final judgment (in Chinese) is available at [http://www.court.gov.cn/xwzx/yw/201410/t20141016\\_198470.htm](http://www.court.gov.cn/xwzx/yw/201410/t20141016_198470.htm), last visited on 27 October 2014..

<sup>260</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 258, Para 25. The Guangdong Court judgment, *supra* note 259, Para 185.

<sup>261</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 258, Para 219.

<sup>262</sup> The Guangdong Court judgment, *supra* note 259, Para 200.

switching cost to sticking to the original software and paying for the basic services.<sup>263</sup> This conclusion could be drawn from the China Internet Network Information Centre's *China Instant Messaging User Research Report*, which concludes that up to 60.6 percent of IM software users in China would not continue using the same software if they have to pay for the basic services.<sup>264</sup> In order to support this viewpoint, the Guangdong Court quoted EU Commission's finding in *Microsoft/Skype* where it observed that more than 75 percent of Skype users "would cease using its free service if it started charging for it".<sup>265</sup>

## 3.2 Problems before the competition authorities

### 3.2.1 Inter-authority problems

The enforcement issue sits at the heart as to whether a system of competition law could succeed. Although the enforcement authorities and Chinese courts have in some individual cases demonstrated their willingness to imitate successful approaches of advanced economies like the EU, more problems arise when the law is implemented by either the administrative authorities or the courts.

As to enforcement by the administrative authorities, in drafting the AML the policymakers considered to keep the multiple competition law enforcement authorities in order to avoid power struggle and enact the AML smoothly and quickly.<sup>266</sup> As one Chinese competition law scholar put it, "[n]o country in the world appoints so many administrative departments to enforce a law to protect market competition. Without a unified and authoritative law enforcement organization, the anti-monopoly law will be difficult to enforce."<sup>267</sup> It could be possible that three enforcement authorities accumulate enforcement experience at different paces, if one authority has more resources and stronger interests in implementing the AML while other(s) may be not.<sup>268</sup> One commentator contends that the *status quo* would result in 'free-rider problem', namely any enforcement authority might not on its own initiative take

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<sup>263</sup> Ibid, Para 179.

<sup>264</sup> China Internet Network Information Centre's *China Instant messaging User Research Report* (2009), available at <http://www.cnnic.net.cn/hlwfzyj/hlwxzbg/201106/P020120709345301865898.pdf>, last visited on 29 October 2013, p29.

<sup>265</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 258, Para 13, 76 and 121.

<sup>266</sup> See *supra* section 3.1 The enforcement regime.

<sup>267</sup> Li Liu, 'Anti-monopoly Draft Provokes Debate', China Daily, 15 November 2006, available at [http://www.chinadaily.com.cn/china/2006-11/15/content\\_733279.htm](http://www.chinadaily.com.cn/china/2006-11/15/content_733279.htm), last visited on 12 December 2013.

<sup>268</sup> Compared to MOFCOM's active performance in merger control, the NDRC and the SAIC performed to be quite silent. However, since 2013 the NDRC and the SAIC, particularly the former, are speeding up their enforcement against anti-competitive agreements and abusive behaviour.



action but rely on the other two to enforce the Law.<sup>269</sup> It has however been proved to be an unnecessary worry, since theoretically the enforcement power has been explicitly divided among three authorities so in practice it is not reasonable to expect other authorities to cross the line and take action beyond their limits. In spite of this, such division of enforcement power however has resulted in many problems in the long term.<sup>270</sup>

First of all, multiple enforcement authorities could result in less authority and inconsistency.<sup>271</sup> Like some dissonance between the US Federal Trade Commission and the Department of Justice Antitrust Division regarding single-firm conducts,<sup>272</sup> the AML enforcement authorities might have divergent priorities in implementing competition rules due to their different roles in the Chinese government.<sup>273</sup> It could, partly, be demonstrated by their inconsistent implementing rules.<sup>274</sup> It is particularly noticeable between rules adopted by the SAIC and the NDRC, both of whom oversee the realms of anti-competitive agreements and abusive behaviour.<sup>275</sup> As to the former realm, for instance, the SAIC and the NDRC stipulate different conditions for finding unlawful concerted actions. For price-related concerted actions, the NDRC will mainly examine whether the suspected undertakings' actions are consistent and whether there was communication between the suspected undertakings.<sup>276</sup> For non price-related concerted actions, on the other hand, the SAIC's approach is more lenient. Even these two conditions are met, the SAIC will not find concerted

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<sup>269</sup> See Jared A. Berry, 'Anti-Monopoly in China: A Socialist Market Economy Wrestles with Its Antitrust Regime' (2005) 2 *International Law and Management Review* 129, p150.

<sup>270</sup> See Maher M Dabbah, 'The Development of Sound Competition Law and Policy in China: An (Im)possible Dream', (2007) 30(2) *World Competition* 341, p356.

<sup>271</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.104-105; Xiaoye Wang, 'Highlights of China's New Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 133, p145.

<sup>272</sup> See Press Release, US Federal Trade Commission, FTC Commissioners React to Department of Justice Report, Competition and Monopoly: Single-Firm Conduct under Section 2 of the Sherman Act, 8 September 2008, available at <http://www.ftc.gov/news-events/press-releases/2008/09/ftc-commissioners-react-department-justice-report-competition-and>, last visited on 28 December 2013.

<sup>273</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.104-105.

<sup>274</sup> See Jared A. Berry, 'Anti-Monopoly in China: A Socialist Market Economy Wrestles with Its Antitrust Regime' (2005) 2 *International Law and Management Review* 129, p150.

<sup>275</sup> See Mark William, Chapter 4 'China' in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p112.

<sup>276</sup> *Provisions against Price Fixing*, *supra* note 232, Article 6.

actions illegal if the undertakings could justify their consistent behaviour.<sup>277</sup> The difference between the SAIC and the NDRC's implementing rules with regard to leniency program could serve as another example in the anti-competitive agreements cases.<sup>278</sup> With respect to dominance abuse cases, one observer found it perhaps inevitable that different approaches would be applied by the NDRC and the SAIC, for example, in defining relevant market and evaluating market power, leading to inconsistent results when investigating price-related and non price-related abuses.<sup>279</sup> For the undertakings, it could be difficult and costly to follow inconsistent implementing rules of different enforcement authorities.<sup>280</sup> The decentralization of AML enforcement power might aggravate the inconsistency in implementing the law. The enforcement authorities at the central level may empower corresponding authorities at the

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<sup>277</sup> *Provisions on the Prohibition of Monopolistic Agreements*, *supra* note 235, Article 3.

<sup>278</sup> The SAIC and the NDRC have different provisions with respect to whether and to what extent the first reporter, the agreement organizer, other reporters would be exempted from punishment. The SAIC provides in its *Provisions on the Prohibition of Monopolistic Agreements*, *supra* note 235, Article 12: "The first business operator that voluntarily reports a monopolistic agreement, provides key evidence and comprehensively and voluntarily cooperates with the investigation *shall be exempted from punishment*. Other business operators that voluntarily reports information about a monopolistic agreement and provide key evidence can be given a mitigation of punishment in light of the actual circumstances." (emphasis added). In the *Provisions on the Procedures for the Administrative Departments for Industry and Commerce to Investigate and Handle Cases of Monopolization Agreements and Abuse of Dominant Market Position*, *supra* note 236, the SAIC provides in Article 20: "For any business operator who voluntarily reports the relevant information on reaching the monopoly agreement and provides important evidence, the administrative department for industry and commerce may, in light of the concrete circumstances, impose a mitigated punishment or exempt it from punishment. The provisions in the preceding paragraph *shall not be applicable to the organizer* of a monopoly agreement." (emphasis added)

The NDRC, on the other hand, provides in its *Provisions on the Administrative Procedures for Law Enforcement against Price Fixing*, *supra* note 233, Article 14: "Where a business operator voluntarily reports the relevant information on its conclusion of a price fixing agreement to the competent price department of the government and provides important evidence, the competent price department of the government may reduce the punishment on it or exempt it from punishment, as the case may be. A business operator which is the first to voluntarily report the relevant information on its conclusion of a price fixing agreement and provides importance evidence *may be exempted from punishment*. A business operator which is the second to voluntarily report the relevant information on its conclusion of a price fixing agreement and provides important evidence may be given a punishment reduced by *not less than 50%*. Any other business operator which voluntarily reports the relevant information on its conclusion of a price fixing agreement and provides important evidence may be given a punishment reduced by *not more than 50%*." (emphasis added)

<sup>279</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.104-105.

<sup>280</sup> See Jared A. Berry, 'Anti-Monopoly in China: A Socialist Market Economy Wrestles with Its Antitrust Regime' (2005) 2 *International Law and Management Review* 129, p150.

provincial level to be responsible for the enforcement work of the AML.<sup>281</sup> Among the three enforcement authorities, the MOFCOM is the only one that remains all decision-making power at the central level, leaving provincial authorities merely the responsibility of case facts investigation.<sup>282</sup> As to the enforcement power division between the other two agencies and their subordinate authorities at the provincial level, while the NDRC authorizes competent subordinate agencies to be responsible for the AML enforcement within their administrative regions<sup>283</sup>, the SAIC may only authorize competent subordinate provincial agencies to be responsible for decision-making of the non price-related cases *on a case-by-case basis*.<sup>284</sup> Such simple and immature decentralization rules seem far from the EU's mechanisms that divide jurisdiction over competition cases between EU Commission and Member States. The EU has established a regime under Regulation 1/2003 which shares EU Commission's competence with national competition authorities and national courts to apply Article 101 and 102 TFEU.<sup>285</sup> The EU has also a jurisdiction division regime under Merger Regulation 139/2004 – and a number of Commission Notices as well<sup>286</sup> – which clearly provides under which circumstances a concentration has a EU dimension,<sup>287</sup> under which circumstances case referrals of concentrations having a EU dimension by the Commission to the competent authorities of the Member States<sup>288</sup> and case referrals of concentrations not having a EU dimension by Member States to the Commission may be made<sup>289</sup>. The gap between EU and China has raised concern as to how competition rules could be implemented in a consistent way between the enforcement authorities at the national level, particularly the SAIC and the NDRC, and their provincial authorities.<sup>290</sup>

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<sup>281</sup> AML, *supra* note 9, Article 10.

<sup>282</sup> *Interim Measures for Investigating and Handling Failure to Legally Declare the Concentration of Business Operators*, *supra* note 227, Article 3.

<sup>283</sup> *Provisions on the Administrative Procedures for Law Enforcement against Price Fixing*, *supra* note 233, Article 3.

<sup>284</sup> *Provisions on the Procedures for the Administrative Departments for Industry and Commerce to Investigate and Handle Cases of Monopolization Agreements and Abuse of Dominant Market Position*, *supra* note 236, Article 3.

<sup>285</sup> *Council Regulation No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Article 81 and 82 of the Treaty*, [2003] OJ L1/1, Article 3.

<sup>286</sup> E.g. *Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings* [2008] OJ C 95/1; *Commission Notice on Case Referral in respect of concentrations* [2005] OJ C 56/2.

<sup>287</sup> *Council Regulation No 139/2004 of 20 January 2004 on the control of concentrations between undertakings*, [2004] OJ L 24/1, Article 1 and 21.

<sup>288</sup> *Ibid*, Article 4(4) and 9.

<sup>289</sup> *Ibid*, Article 4(5) and 22.

<sup>290</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p108.

The second inter-authority problem might be the potential conflict of jurisdiction among administrative authorities, in particular between the SAIC and the NDRC. The simple rule dividing the enforcement power between the NDRC and the SAIC in the realm of anticompetitive agreements and abusive behaviour may cause potential conflict in enforcement. Regarding abuse of dominance, for example, the NDRC is in charge of issues related to unfairly high or low prices, refusal to deal by setting unfairly high or low prices, exclusive dealing through price discounts, the imposition of unreasonable fees in addition to sales price, and price-related discriminatory treatment.<sup>291</sup> The SAIC, on the other hand, is responsible for issues related to refusal to deal, exclusive dealing, bundling and tying, and discriminatory treatment through non price-related transaction terms.<sup>292</sup> For one thing, an undertaking could be involved in a mixture of anti-competitive conducts over which both authorities have jurisdiction, and it is not clear how to settle such concurrent jurisdiction.<sup>293</sup> For another, it could be problematic even there is only one type of anti-competitive behaviour involved. As to the refusal to license issue particularly, based on the aforementioned power division, it could be reached that the NDRC is responsible for refusal to license by setting unfair price, while other unconditional refusal to license cases are assigned to the SAIC. A conflict of jurisdiction would arise in this sense since it is not always that easy to identify whether the behaviour at issue is price-related or non price-related.<sup>294</sup> With respect to this potential dispute, the SAIC and the NDRC have allegedly reached an internal consensus that once a case has been accepted by either agency then the other will refuse to hear the same complaint.<sup>295</sup> However this arrangement may cause inconsistent results for similar cases. Within Chinese competition law enforcement regime, the Anti-Monopoly Committee of the State Council is responsible for

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<sup>291</sup> *Provisions against Price Fixing*, *supra* note 232, Articles 11-16.

<sup>292</sup> *Provisions on the Prohibition of Abuse of Dominant Position*, *supra* note 234, Articles 4-7.

<sup>293</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, p641; Xiaoye Wang, 'The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress' (2009) 54 *The Antitrust Bulletin* 579, p590.

<sup>294</sup> See Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p264; Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p33; Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p104; Mark William, Chapter 4 'China' in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p113.

<sup>295</sup> See Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p33.

coordinating the enforcement work among the enforcement authorities.<sup>296</sup> However, it is not clear how the Anti-Monopoly Committee would perform its function with regard to the jurisdictional conflict.<sup>297</sup> The appointment of the members of the Anti-Monopoly Committee on the one hand involves other central ministries and committees in mitigating the inter-authority conflicts, leaving the disputes beyond the Committee itself to the State Council level and thus including other industrial policy concerns; on the other hand, it might be possible that the enforcement of the AML by the SAIC and the NDRC will be unduly influenced by the MOFCOM since the latter, apart from being a member in the Committee, also undertakes the day-to-day work for the Committee.<sup>298</sup>

It is contended that the complex institutional enforcement framework with multiple competition authorities might “boost” the private enforcement of the AML in China.<sup>299</sup> Nevertheless, it has been proved not right. The figure released by the Chinese Supreme Court demonstrates that by the end of 2011 the private enforcement has not yet boosted up with merely 61 anti-monopoly civil lawsuits accepted by the Chinese courts since August 2008.<sup>300</sup> But the amount of first instance civil cases involving anti-monopoly disputes in the year 2012 surprisingly increased up to 55.<sup>301</sup> It appears that the reason behind the accelerated development of the private enforcement of the AML is thus not the complex administrative enforcement system, but might be the AML judicial interpretation, release of which increases the predictability of the civil anti-monopoly lawsuits. It is also claimed that the *status quo* division of enforcement power could generate competition among three administrative

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<sup>296</sup> AML, *supra* note 9, Article 9.

<sup>297</sup> *The Working Rules of the Anti-Monopoly Committee of the State Council* (adopted by the first meeting of the Anti-Monopoly Committee of the State Council 13 September 2008) specifies the composition and working rules of the Committee. It confirms that the plenary meeting and the director meeting should coordinate the dispute between the administrative agencies in enforcing the AML, while there is no substantive rule as to how the Anti-Monopoly Committee will deal with the possible jurisdiction conflict. (See press release at [http://news.xinhuanet.com/politics/2008-09/13/content\\_9982466.htm](http://news.xinhuanet.com/politics/2008-09/13/content_9982466.htm), last visited on 20 January 2014, however full text of this Working Rules is not available online.)

<sup>298</sup> See Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, pp.106-107.

<sup>299</sup> Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, p267.

<sup>300</sup> See interview with Xiangjun Kong, President of the IP tribunal under the Supreme Court, in his answers to reporters’ questions on the first judicial interpretation of the AML, available at [http://news.xinhuanet.com/legal/2012-05/08/c\\_111910772.htm](http://news.xinhuanet.com/legal/2012-05/08/c_111910772.htm) (in Chinese), last visited on 20 January 2014.

<sup>301</sup> See *Intellectual Property Protection by Chinese Courts in 2012* (White Paper), issued by Chinese Supreme Court on 22 April 2013, English version is available at [http://www.court.gov.cn/zscq/bhcg/201304/t20130426\\_183662.html](http://www.court.gov.cn/zscq/bhcg/201304/t20130426_183662.html), last visited on 20 January 2014.

authorities, “increase the output and improve the quality” of the enforcement, and avoid weaker competition law enforcement that might otherwise occurred in a single enforcement authority system.<sup>302</sup> However, the main stream suggestion in light of the foregoing inter-authority shortcomings within the current enforcement system is that China should establish an independent Anti-Monopoly enforcement agency under the State Council at the ministry level.<sup>303</sup>

### 3.2.2 Intra-authority problems

In addition to the inter-authority problems, some intra-authority shortcomings also contribute to the inefficient enforcement of the AML. Low hierarchy is the first problem. The administrative level of these enforcement authorities within the Chinese administrative system is not sufficiently high, leading to their less independence and authority.<sup>304</sup> In 2008 the merger between China Unicom and China Netcom, the two leading telecommunication SOEs, could illustrate that the enforcement authorities lack sufficient authority due to their lower positions in the administrative system. Although according to the scale of this telecom merger case it should have been notified to the MOFCOM for approval, the MOFCOM officials admitted that they did not receive such merger notification from the parties.<sup>305</sup> While the undertakings claimed that the merger was already approved by their supervisory authority – the Ministry of Industry and Information Technology which is at the same administrative level with MOFCOM, it was difficult for the Anti-Monopoly Bureau (a division under the MOFCOM), or even the MOFCOM itself, to challenge another ministry’s decision.<sup>306</sup> Another reason resulting in MOFCOM’s reluctance to take action might be that the parties to the transaction are central-administered SOEs whose principals are at the same (or similar) administrative level with the minister of the MOFCOM in the Chinese administrative

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<sup>302</sup> Angela Huyue Zhang, ‘The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective’ (2011) 56(3) *The Antitrust Bulletin* 631, pp.644-645.

<sup>303</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, ‘China’s Competition Policy Reforms: The Anti-Monopoly Law and Beyond’ (2008) 75 *Antitrust Law Journal* 231, pp.261-262; Jared A. Berry, ‘Anti-Monopoly in China: A Socialist Market Economy Wrestles with Its Antitrust Regime’ (2005) 2 *International Law and Management Review* 129, p150; Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p99. See chapter 5 for more detailed analysis in this respect.

<sup>304</sup> Xiaoye Wang, ‘The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress’ (2009) 54 *The Antitrust Bulletin* 579, p590.

<sup>305</sup> See MOFCOM confirmed that China Unicom / China Netcom merger is suspected of infringing the Anti-Monopoly Law, Economic Observer, 1 May 2009, available at <http://money.163.com/09/0501/09/587HV23500252KFB.html> (in Chinese), last visited on 20 January 2014.

<sup>306</sup> See Angela Huyue Zhang, ‘The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective’ (2011) 56(3) *The Antitrust Bulletin* 631, p651.

system.<sup>307</sup> Similar challenges will also confront the NDRC and the SAIC when powerful SOEs are involved in cases related to anti-competitive agreements or abusive behaviour.

In the second place, the decisions delivered by Chinese enforcement authorities lack transparency and intra-authority consistency. It is vital that undertakings should be informed of the enforcement authorities' decisions in order to establish their clear expectations as to how the AML would be enforced. Article 30 of the AML requires the MOFCOM to publish, in a timely manner, its decisions prohibiting or conditionally approving the concentrations notified.<sup>308</sup> Apart from these cases, the MOFCOM has the discretion to determine whether or not to publish its unconditional clearance decisions. For other two enforcement authorities, they are even entitled to selectively publish their enforcement decisions since article 44 of the AML provides that they "may publish" their decisions rather than "must publish".<sup>309</sup> Moreover, for the decisions published, the written decisions released are normally brief, conclusory, with little substantive legal reasoning and analysis – although being progressively improved to some extent.<sup>310</sup> In the absence of concrete analysis articulating the rationale for specific decisions, it is impossible for the outside observers to evaluate how the authorities understand the AML, interpret the rules into specific cases, and connect available evidences with their published

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<sup>307</sup> See MOFCOM confirmed that China Unicom / China Netcom merger is suspected of infringing the Anti-Monopoly Law, Economic Observer, 1 May 2009, available at <http://money.163.com/09/0501/09/587HV23500252KFB.html> (in Chinese), last visited on 20 January 2014.

<sup>308</sup> AML, *Supra* note 9, Article 30.

<sup>309</sup> Ibid, Article 44. Among the three Anti-Monopoly Law enforcement authorities, the MOFCOM does the best on the information release as it already has established its enforcement information disclosure mechanism. For the merger cases that have been cleared without conditions, the MOFCOM will release a list per quarter since the fourth quarter of 2012 (information updated on <http://fldj.mofcom.gov.cn/article/zcfb/>); for the merger cases that have been cleared subject to conditions or have been banned, the MOFCOM will publish the full text of its decision on its official website (information updated on <http://fldj.mofcom.gov.cn/article/ztxx/>). The SAIC has also made a major step forward on the enforcement information disclosure as it published the decisions (in full text) of 12 closed anti-competitive agreements cases (out of 24 cases in total since the effective of the AML) on July 26 2013 before the fifth anniversary of the implementation of the AML, available at <http://www.saic.gov.cn/zwgk/gggs/jzzf/>, last visited on 20 January 2014. As to the enforcement of the AML by the NDRC, on 2 September 2014, the NDRC *for the first time* published the full decisions in Zhejiang Car Insurance Catel case imposing combined fines of RMB 110 million (USD 17.89 million) on a local trade association in Zhejiang province and 23 property insurance companies for their price fixing behaviour, decisions (in Chinese) are available at <http://jjs.ndrc.gov.cn/fjld/index.html>, last visited on 10 October 2014.

<sup>310</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, pp.123-124; Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, pp.652-653; Mark William, Chapter 4 'China' in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p114.

findings.<sup>311</sup> It is understandable that it is not a tradition for the officials of Chinese administrative authorities, like the judges in Chinese courts,<sup>312</sup> to write long decisions and to explain how the decisions are made in details. But the public oversight on administrative decision-making and predictability of undertakings' commercial behaviour would thus be jeopardized if the enforcement authorities continue disclosing insufficient information merely with the purpose of avoiding the exposure of any mistake that might be used against the authority in future cases.<sup>313</sup> In addition, to allow undertakings to estimate potential public intervention beforehand, each enforcement authority should keep its decisions consistent. In other words, the AML enforcement authorities should "to some extent be bound by its prior decisions and reasoning."<sup>314</sup> Otherwise, undertakings could not predict the possible consequences of their commercial decisions if the authorities can decide a case disregard the prior decisions in which similar facts have been analyzed in the recent past.

In the third place, the shortage of personnel serves as another main reason for the unproductive enforcement of the AML. In the US, in 2006 there were 779 employees, including 565 professional staff members such as attorneys and economists, working for the Antitrust division of the Department of Justice.<sup>315</sup> In the Federal Trade Commission, by the end of 2012 there were over 1100 employees, including 613 attorneys and 77 economists.<sup>316</sup> As to the EU Commission, in 2011 there were around 900 staff members working in the DG Competition responsible for monitoring competition issues in the EU market.<sup>317</sup> Japan's Fair Trade Commission had 799 staff members including 456 investigators in 2012.<sup>318</sup> South Korea's Fair Trade Commission had more than 500 employees in 2011.<sup>319</sup> However, the most well-equipped Chinese enforcement authority is the MOFCOM, which has only around 30 staff members in

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<sup>311</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p124.

<sup>312</sup> See *infra* note 330.

<sup>313</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, pp.653-654.

<sup>314</sup> Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p263.

<sup>315</sup> See Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed.) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p37.

<sup>316</sup> Data from <http://www.ftc.gov/opp/gpra/2012parreport.pdf>, last visited on 20 January 2014.

<sup>317</sup> Data from [http://ec.europa.eu/dgs/competition/factsheet\\_general\\_en.pdf](http://ec.europa.eu/dgs/competition/factsheet_general_en.pdf), last visited on 28 November 2013.

<sup>318</sup> Data from [http://www.jftc.go.jp/en/about\\_jftc/statistics.html](http://www.jftc.go.jp/en/about_jftc/statistics.html), last visited on 20 January 2014.

<sup>319</sup> Data from 2012 *Annual Report of Fair Trade Commission of Republic of Korea*, available at [http://eng.ftc.go.kr/bbs.do?command=getList&type\\_cd=53&pageId=0301](http://eng.ftc.go.kr/bbs.do?command=getList&type_cd=53&pageId=0301), last visited on 20 January 2014, p14.



the Anti-Monopoly Bureau.<sup>320</sup> Though it is worth noting that an economic division has been established under the Anti-Monopoly Bureau and it undertakes the economic analysis in reviewing merger cases, the profiles of the staff members have not been disclosed.<sup>321</sup> The NDRC's Bureau of Price Supervision and Anti-Monopoly has more than 20, but less than 30 staff members.<sup>322</sup> The situation of the SAIC is even worse. There are less than ten full-time personnel in the Anti-Monopoly and Anti-Unfair Competition Bureau at the national level.<sup>323</sup> Top officials of Chinese competition law enforcement authorities admitted that up to September 2014 there are merely around fifty full-time competition law staff members in total within three authorities.<sup>324</sup> Even these full-time staff members are equipped with requisite competition skills and sufficient economic knowledge, it would be too difficult for them, if not impossible, to handle the heavy workload and analyse each case, particularly those complicated and novel issues, with adequate caution. Take merger control for example, until August 2014 – six years enforcement since the enactment of the AML in August 2008, there are 945 merger cases registered in the MOFCOM of which the number of cases the MOFCOM completed the competition review is 875.<sup>325</sup> Apparently the workload would be too heavy for a bureau with

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<sup>320</sup> See Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed.) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p37.

<sup>321</sup> See Interview with Ming Shang, Director General of the Anti-Monopoly Bureau under the MOFCOM, February 2011, available at [http://www.americanbar.org/content/dam/aba/migrated/2011\\_build/antitrust\\_law/feb11\\_shangintrvw2\\_23f.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/migrated/2011_build/antitrust_law/feb11_shangintrvw2_23f.authcheckdam.pdf), last visited on 20 January 2014, at 4.

<sup>322</sup> See Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed.) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p37. The Bureau of Price Supervision and Anti-Monopoly was authorised by the State Commission Office for Public Sector Reform on 27 July 2011 to increase its personnel from current 26 to 46 (maximum), see Beijing Bar Association (ed.) *Legal Practice of Anti-monopoly and Anti-unfair competition* ('反垄断与反不正当竞争法律实务精解') (Peking University Press 2012), p243. As mentioned above, the NDRC in general authorizes its subordinate provincial agencies to enforce the AML in their administrative regions, therefore these provincial agencies are allowed to increase in total 150 personnel, see Kunlin Xu, 'New developments in Price-related enforcement of the Anti-monopoly Law' in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed.) *Report on Competition Law and Policy of China 2012* (Law Press, China, 2013) 7, pp.7-8.

<sup>323</sup> Ibid.

<sup>324</sup> See Chinese competition law authorities' briefing on 11 September 2014, available at [http://www.china.com.cn/zhibo/2014-09/11/content\\_33487367.htm?show=t](http://www.china.com.cn/zhibo/2014-09/11/content_33487367.htm?show=t) (in Chinese), last visited on 12 September 2014.

<sup>325</sup> Data from the briefing jointly held by three Chinese competition law authorities on 11 September 2014, available at [http://www.china.com.cn/zhibo/2014-09/11/content\\_33487367.htm?show=t](http://www.china.com.cn/zhibo/2014-09/11/content_33487367.htm?show=t) (in Chinese), last visited on 12

merely about 30 staff members, if compared to other advanced economies, such as the EU. The EU Commission received more than 1400 notifications from 2009 to 2013.<sup>326</sup> Though it exceeds the figure in China by about 450 – which is not a small number, the personnel shortage of the MOFCOM is evident, considering the wide manpower gap between EU commission and Chinese merger reviewer and the (still) increasing number of concentration notifications in China.

### 3.3 Problems before the courts

It is believed that the AML apparently rely on the administrative enforcement system rather than the judicial system to handle anti-monopoly cases.<sup>327</sup> This is, partly due to the fact that three administrative enforcement authorities already handled competition issues prior to the enactment of the AML. After all, the public enforcement of the AML should play the primary role in implementing the competition policies. Judges are less informed about particular industries while administrative officials of the public enforcement authorities have devoted themselves to studying competition issues in the areas supervised by these authorities.<sup>328</sup> In other words, judges to some extent are generalists while administrative officials are specialists.

Relying on the administrative authorities to enforcement the AML is also the result of the limited capabilities of the Chinese judicial system. Some doubt has been cast on the designated Chinese courts' ability to implement the AML since generally speaking the judges have insufficient training in competition law and economics.<sup>329</sup> Moreover, China is a civil law

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September 2014. According to the written record of this briefing, 849 cases were cleared unconditionally, 4 cases were cleared with conditions and 2 cases were rejected. But apparently the amount of cases cleared with conditions is wrong in this briefing. According to MOFCOM website (<http://fldj.mofcom.gov.cn/article/ztxx/>?), the amount of conditionally cleared merger cases should be 24, otherwise the total amount of completed merger cases would not be 875.

<sup>326</sup> The statistics of EU merger cases could see <http://ec.europa.eu/competition/mergers/statistics.pdf>, last visited on 27 January 2014.

<sup>327</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p264.

<sup>328</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, p656.

<sup>329</sup> See H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, pp.214, 226-227. See also Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p242; Subrata Bhattacharjee, 'The Merger Review Process under the New PRC Anti-Monopoly Law: Selected Issues' (2008) *A.B.A. Section Antitrust* 9 (presenting at the New Chinese Anti-Monopoly Law Teleseminar, 23 January 2008); Mark William, Chapter 4 'China' in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p96.

country where there is no place for ‘judge-made’ law. Like administrative authorities’ brief and conclusory decisions, Chinese judges are not used to writing detailed opinions. Against the background of the vague AML, undertakings could not foresee what courts will do under a particular circumstance without binding precedents under similar circumstances.<sup>330</sup> Consequently, a modern competition culture in China is difficult to be established as long as Chinese courts are not capable of understanding and interpreting, in a consistent way, the careful drafting competition policies, as well as guidelines and decisions adopted by the Anti-Monopoly Committee and the enforcement authorities.<sup>331</sup>

On top of these general shortcomings which make it difficult to establish a competition culture through judicial branch, the quality and quantity of the judicial review cases and the civil anti-monopoly cases have been respectively influenced by some other factors. As to the judicial review of an administrative decision pursuant to the *Administrative Procedure Law*<sup>332</sup>, defendants might not be willing to lodge an appeal owing to the complicated procedures of administrative litigation and, more importantly, the persistent bias of the Chinese courts in favour of government authorities.<sup>333</sup> The Chinese courts are perceived as being lack of independence and influenced by local governments which favour local enterprises (*inter alia* SOEs located in that region) in competition with the defendant, creating the perception that it is meaningless for the defendant to seek for judicial review.<sup>334</sup> As to the private enforcement, the limited amount of civil litigations is due to the fact that the burden of proof imposed on the plaintiff is difficult to satisfy. This is partly because of the lack of an adequate discovery system in relevant civil procedural laws so the plaintiffs have problem in collecting evidence, and partly because of the plaintiffs’ lack of understanding of competition law therefore they might

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<sup>330</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, ‘China’s Competition Policy Reforms: The Anti-Monopoly Law and Beyond’ (2008) 75 *Antitrust Law Journal* 231, p242.

<sup>331</sup> H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p227.

<sup>332</sup> *Administrative Procedure Law of the People’s Republic of China* (adopted by the National People’s Congress, issued on 4 April 1989 and effective since 1 October 1990, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=1204&lib=law&SearchKeyword=&SearchCKeyword=%D0%D0%D5%FE%CB%DF%CB%CF%B7%A8>, last visited on 20 January 2014)

<sup>333</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, ‘China’s Competition Policy Reforms: The Anti-Monopoly Law and Beyond’ (2008) 75 *Antitrust Law Journal* 231, p241; H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p226.

<sup>334</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p226.

not be able to provide sophisticated economic analysis to support their claims.<sup>335</sup> Therefore the chance to win a civil anti-monopoly case is slim. So far in China there has been only two civil anti-monopoly cases reported in which the plaintiffs won the cases.<sup>336</sup>

#### 4. EU – China cooperation

As a result of the Joint Statement adopted at the EU-China Summit of 5 September 2001 which included competition policy within the framework<sup>337</sup>, on 6 May 2004 DG Competition of European Commission and the MOFCOM signed *Terms of Reference of the EU-China Competition Policy Dialogue*.<sup>338</sup> The Competition Policy Dialogue, according to *the Terms of Reference*, aims to “establish a permanent mechanism of consultation and transparency between China and the EU in this area, and to enhance the EU’s technical and capacity-building assistance to China in the area of competition policy.”<sup>339</sup> It is the first time that the EU Commission has adopted the form of an informal dialogue at the bilateral level in the internationalization of EU competition law. With no legally binding obligations on either side, it is possible to set up a permanent and flexible forum for the EU Commission on the one side, and the Chinese competition law administrative authorities on the other side, to undertake communication and consultation. On 20 September 2012 DG Competition and other two Chinese enforcement authorities – the NDRC and the SAIC – signed a *Memorandum of Understanding on Cooperation in the area of Anti-Monopoly Law*, the

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<sup>335</sup> See Angela Huyue Zhang, ‘The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective’ (2011) 56(3) *The Antitrust Bulletin* 631, pp.657-660. See also Youngjin Jung and Qian Hao, ‘The New Economic Constitution in China: A Third Way for Competition Regime’ (2003) 24(1) *Northwestern Journal of International Law & Business* 107, p165.

<sup>336</sup> The first case where the plaintiff won is *Rainbow vs. Johnson & Johnson*, a vertical price fixing agreement case. The judgment was issued by Shanghai High Court on 1 August 2013, full text of the judgment is available at <http://www.hshfy.sh.cn:8081/flws/text.jsp?pa=ad3N4aD01JnRhaD2jqDIwMTKjqbumuN/D8cj9KNaqKdbV19a12jYzusUmd3o9z> (in Chinese), last visited on 20 December 2013. Press release on this case, as well as the general information of private enforcement of the AML within the Shanghai court system, is available at <http://www.hshfy.sh.cn/shfy/gweb/xxnr.jsp?pa=aaWQ9Mjc5NjgwJnhoPTEPdcssz> (in Chinese), last visited on 20 December 2013. The second civil anti-monopoly case in favour of the plaintiff is a horizontal agreement case, a ruling issued by Beijing No.2 Intermediate Court on 21 November 2013 against Beijing Seafood Wholesale Industry Association, full text of the judgment is not published, press release available at <http://bj2zy.chinacourt.org/public/detail.php?id=1152>, (in Chinese), last visited on 29 January 2014.

<sup>337</sup> Joint Press Statement adopted between the EU and China at the Fourth EU-China Summit, Brussels, 5 September 2001, see [http://europa.eu/rapid/press-release\\_PRES-01-312\\_en.htm](http://europa.eu/rapid/press-release_PRES-01-312_en.htm), last visited on 20 January 2014.

<sup>338</sup> *Terms of Reference of the EU-China Competition Policy Dialogue*, see [http://ec.europa.eu/competition/international/bilateral/cn2b\\_en.pdf](http://ec.europa.eu/competition/international/bilateral/cn2b_en.pdf), last visited on 20 January 2014.

<sup>339</sup> Ibid.

objective of which is to strengthen cooperation and coordination between the EU and China in the areas of matters covered by the AML regarding anticompetitive agreements and the abuse of dominant market positions, excluding matters relating to mergers.<sup>340</sup>

In implementing foregoing bilateral agreements in competition policy area, EU-China Competition week has been selected as one significant form to provide technical assistance from EU Commission to meet the current needs of Chinese competition authorities.<sup>341</sup> So far, EU-China Competition weeks have been jointly hosted by DG Competition and Chinese competition authorities in China for nine times.<sup>342</sup> A series of workshops, conferences, roundtables, and seminars have been organized on the subjects of mergers, abuse of dominance, anti-competitive agreements, state aid, competition policy and IPRs, remedy issues and investigative techniques.<sup>343</sup> Officials from DG Competition of EU Commission and Member States' competition authorities have shared EU successful experience on these issues, and hundreds of Chinese officials from the three competition authorities – including agencies at the national level and also the provincial level – have participated and benefited from these training sessions. All training materials delivered throughout these Competition weeks are accessible within the internal training network of Chinese competition authorities for those who could not attend the specific training sessions. Apart from the training sessions held in the EU-China Competition weeks, numerous high-level conferences have been organized to share European best practice and experience in enforcing competition rules with not only competition authorities' officials but also Chinese judges.<sup>344</sup> By fostering a EU-like

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<sup>340</sup> *Memorandum of Understanding on Cooperation in the area of Anti-Monopoly Law*, see [http://ec.europa.eu/competition/international/bilateral/mou\\_china\\_en.pdf](http://ec.europa.eu/competition/international/bilateral/mou_china_en.pdf), last visited on 20 January 2014.

<sup>341</sup> On the part of the EU Commission's enforcement, the bilateral cooperation in DG COMP's antitrust and merger case investigations with China in 2012-2013 accounts for 8 percent in total by the amount of cases, As to merger cases in particular, there have been 7 cases (15 percent in all EU merger cases with international cooperation) where China cooperated with the EU Commission. Data disclosed by Mrs Blanca Rodriguez Galindo (Head of the International Relations Unit, DG COMP) in her keynote speech at the seminar *Global Antitrust Hot Topics: EU, US & Global Perspective*, Brussels, 25 September 2014.

<sup>342</sup> For more information on the EU-China Competition Weeks see <http://www.euchinacomp.org/index.php/competition-weeks/62-competition-weeks>, last visited on 29 September 2014. The latest (ninth) EU-China Competition Week ("Workshop on Investigative Techniques in Merger Review") was held by MOFCOM Anti-Monopoly Bureau in Chengdu, China, 20-24 October 2014, press release available at <http://fldj.mofcom.gov.cn/article/xxfb/201410/20141000770472.shtml>, last visited on 23 October 2014.

<sup>343</sup> Ibid.

<sup>344</sup> E.g. *EU-China Workshop on the Abuse of Dominant Market Position in China*, Beijing, 14 January 2009, see the speech of Torben Toft, Principal Administrator of DG Competition at [http://ec.europa.eu/competition/speeches/text/sp2009\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2009_01_en.pdf), last visited on 20 January 2014; *EU-China Conference on the Anti-Monopoly Law*, Dalian, 11 May 2009, see the speech of Torben Toft, principal

competition law model in China, the EU could also be benefited on the grounds that, for one thing the influence of the EU model in the global competition law development would be significantly increased, and for another the obstacles relating to competition law issues in future EU-China trade negotiations could, to a great extent, be removed by such bilateral cooperation.<sup>345</sup>

## 5. Conclusion

Previous analysis has demonstrated that, compared to the US antitrust law, it is the EU competition law that has influenced most aspects of the AML, including the setting of multiple competition law objectives, and most provisions in the three competition law realms of anticompetitive agreements, abuse of dominance and merger review. Based on the comprehensive AML, China has established a two-layer, three-pronged enforcement regime. This EU-like administrative-oriented enforcement regime has adopted sets of procedural and substantial rules to implement the law. However, the vagueness within the competition law legislations and the enforcement authorities' limited experience in practice give rise to an unavoidable result that many competition law issues are unsolved in China, such as the balancing between economic considerations and industrial policy considerations in a given case. Moreover, the current problems within the administrative system (including inter-authority and intra-authority problems) and the judicial system in implementing the AML, and the increasingly close EU-China relationship with respect to competition law, lead to the conclusion that it is highly likely that the EU successful experience, *inter alia* in certain complicated competition issues such as those at the intersection of competition law and IPR, could provide further guidance for China. Thus it is quite natural to speculate whether and to what extent the pattern adopted by the EU Commission and the EU courts to tackle refusal to license IPR, currently a fairly novel issue for China, could influence and contribute to China's future practice in this particular respect.

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Administrator of DG Competition at [http://ec.europa.eu/competition/speeches/text/sp2009\\_10\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2009_10_en.pdf), last visited on 20 January 2014; *EU-China Conference on the Interface between Competition and Intellectual Property Law*, Dalian, 10-11 June 2010, materials of the conference could be accessed at [http://www.ipr2.org/index.php?view=article&id=1204%3Aeu-china-conference-on-the-interface-between-competition-and-intellectual-property-law&option=com\\_content&Itemid=248](http://www.ipr2.org/index.php?view=article&id=1204%3Aeu-china-conference-on-the-interface-between-competition-and-intellectual-property-law&option=com_content&Itemid=248), last visited on 20 January 2014; *EU-China Seminar on Innovation and Competition in the IT Sector*, Beijing, 26 June 2012, <http://www.euchinacomp.org/index.php/competition-weeks?id=241>, last visited on 20 January 2014.

<sup>345</sup> Qianlan Wu, 'EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law' (2012) 18(3) *European Law Journal* 461, p475.

## CHAPTER II EU competition law on refusal to license

### 1. Introduction

The creation of Article 102 TFEU aims to regulate the conducts of dominant undertakings in relevant markets. Its purpose is to prevent the effective competition process in the internal market of European Union ('EU') from being distorted by dominant undertakings' abusive conducts, which could be capable of driving out current competitors or establishing high entry barrier for potential entrants. However, Article 102 TFEU does not prohibit the possession of a dominant position which is legitimately acquired by "superior efficiency or innovativeness".<sup>1</sup>

In the EU it is apparently recognized by the laws of the Member States that an undertaking, even holding a dominant position on a relevant market, in most cases is free to decide its business strategy and to choose its trading partner.<sup>2</sup> Accordingly, with respect to intellectual property right ('IPR'), the EU courts have in a number of cases confirmed that it is at the discretion of the right holder to license, or otherwise to refuse to license, its IPR to a third party, including its competitors.<sup>3</sup> The purpose of Article 102 TFEU, As Advocate General Jacobs stated in his opinion in *Bronner*, "is to prevent distortions of competition – and in particular to safeguard the interests of consumers – rather than to protect the position of particular competitors"<sup>4</sup>. Only under some recognized exceptional circumstances, which have been developed by the EU courts, shall the dominant undertakings be ordered to license their IPRs to new customers or continue their licensing relations with current customers.<sup>5</sup> On this occasion, the essential IPR owned by the dominant undertakings shall, subject to the compulsory licensing, be accessed by the competitors. Otherwise, an abusive refusal to license IPR would lead to limiting competitors' production, or impeding technical development of certain

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<sup>1</sup> Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights* (second edition, Oxford University Press, 2011), p33.

<sup>2</sup> See Judgment in *Oscar Bronner*, C-7/97, ECLI:EU:C:1998:264, opinion of Mr Advocate General Jacobs delivered on 28 May 1998, Para 53 and 56.

<sup>3</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, Para 7-8; Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para. 49; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para. 34; Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 331.

<sup>4</sup> Judgment in *Oscar Bronner* ECLI:EU:C:1998:264, Opinion of Advocate General Jacobs, Para 58. (emphasis added)

<sup>5</sup> Judgment in *Volvo* ECLI:EU:C:1988:477, Para 9; Judgment in *Magill* ECLI:EU:C:1995:98, Para 50; Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 35; Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 319, 330, 331, 332 and 336.

neighbouring market to the prejudice of consumers within the meaning of Article 102 TFEU. The list of abusive practices provided by Article 102 TFEU is not exhaustive and the practices mentioned there are merely examples of abuse of a dominant position.<sup>6</sup> It is therefore controversial that under which conditions an order to license may be applied. This chapter and the next chapter will investigate the EU approach on refusal to license by analyzing *inter alia* the analytical framework respectively adopted by the EU Commission and EU Courts. Apart from the substantial criteria established by the case law in right owner's behaviour of refusal to license, a detailed analysis of related EU competition law principles and concepts is necessary in order to understand the EU model as an integrated system. This not only includes those issues prior to assessment of the allegedly abusive practice, such as defining the relevant market and assessing the existence of dominant position. The latter could be quite complicated and controversial in some 'dynamically competitive industries', such as information technology ('IT') industry, where a high market share may not indicate strong market power. The analysis also investigates other procedural issues that should be considered during or after the Commission's investigation, such as the choice of Article 7 and Article 9 of Regulation 1/2003, and the applicability of behavioural and structural remedies in refusal to license situation.

## 2. The criteria established by the case law of the CJEU

### 2.1 Essential Facility Doctrine

The obligation under competition law to allow one's significant property to be accessed by his competitors always relates to the theory of 'essential facilities'.<sup>7</sup> It is well accepted that the first case on the essential facilities doctrine is the case *United States v Terminal Railroad Association*<sup>8</sup> judged by US Supreme Court. The essential facility doctrine is established to allow the maintenance of competition take precedence over the contractual freedom of

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<sup>6</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, para 860; Judgment in *Deutsche Telekom v Commission*, C-280/08 P, ECLI:EU:C:2010:603, para 173; Judgment in *TeliaSonera*, C-52/09, ECLI:EU:C:2011:83, para 26.

<sup>7</sup> More discussion on this doctrine see, for instance, Barry Doherty, 'Just What are Essential Facilities?' (2001) 38 *Common Market Law Review* 397; Phillip Areeda, 'Essential Facilities: An Epithet in Need of Limiting Principles' (1990) 58 *Antitrust Law Journal* 841; Einer Elhauge, 'Defining Better Monopolization Standards' (2003) 56 *Stanford Law Review* 253; Abbott B. Lipsky and J. Gregory Sidak, 'Essential Facilities' (1999) 51 *Stanford Law Review* 1187; Derek Ridyard, 'Essential Facilities and the Obligation to Supply Competitors under UK and EC Competition Law', (1996) 8 *European Competition Law Review* 234.

<sup>8</sup> *United States v Terminal Railroad Association*, 224 U.S. 383 (1912).



undertakings controlling an important facility.<sup>9</sup> However, the US Supreme Court, in the *Terminal Railroad Association* case, as well as in the following significant cases such as *Associated Press*<sup>10</sup>, *Otter Tail Power Co.*<sup>11</sup> and *Aspen Skiing*<sup>12</sup>, has never clearly explained<sup>13</sup>, or explicitly acknowledged this doctrine.<sup>14</sup> The Supreme Court in 2004 explicitly denied the existence of essential facilities doctrine in *Trinko*<sup>15</sup>. Instead of a general antitrust liability, the Court claimed that the antitrust analysis should always be subject to “the particular structure and circumstances of the industry at issue”.<sup>16</sup> Likewise, many US lawyers and economists have argued to interpret the doctrine in a narrow way.<sup>17</sup>

Whether the essential facilities doctrine in the EU is a clone product of the US theory, or it has its own characters, has been subject to extensive debates.<sup>18</sup> The first essential facility case in

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<sup>9</sup> Vassilis Hatzopoulos, ‘The EC Essential Facilities Doctrine’, in Giuliano Amato and Claus-Dieter Ehlermann (eds.), *EC Competition Law: A Critical assessment* (Hart Publishing, 2007), p333.

<sup>10</sup> *Associated Press v United States*, 326 U.S. 1 (1945).

<sup>11</sup> *Otter Tail Power Co. v United States*, 410 U.S. 366 (1973).

<sup>12</sup> *Aspen Skiing v Aspen Highlands Skiing*, 472 U.S. 585 (1985).

<sup>13</sup> The most commonly cited definition of essential facilities doctrine is from the Court of Appeals in *MCI Communications v. AT&T*, 708 F.2d 1081, (7th Cir. 1983): “The case law sets forth four elements necessary to establish liability under the essential facilities doctrine: (1) control of the essential facility by a monopolist; (2) a competitor’s inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility.” (pp.1132-1133)

<sup>14</sup> See Barry Doherty, ‘Just What are Essential Facilities?’ (2001) 38 *Common Market Law Review* 397, p398. Justice Breyer in his concurring opinion in *AT&T* also stated that the Supreme Court has never adopted this doctrine. *AT&T Corp. v. Iowa Util. Bd.*, 525 U.S. 366, 428 (1999) (concurring opinion).

<sup>15</sup> *Verizon Communications Inc. v Law Office of Curtis V Trinko* (hereinafter ‘*Trinko*’), 540 U.S. 398 (2004).

“[T]his conclusion would be unchanged even if we considered to be established law the “essential facilities” doctrine crafted by some lower courts... We have never recognized such a doctrine... and we find no need either to recognize it or to repudiate it here. It suffices for present purposes to note that the indispensable requirement for invoking the doctrine is the unavailability of access to the “essential facilities”; where access exists, the doctrine serves no purpose.” (p411)

<sup>16</sup> *ibid.*

<sup>17</sup> See e.g. Phillip Areeda, ‘Essential Facilities: An Epithet in Need of Limiting Principles’ (1990) 58 *Antitrust Law Journal* 841; Einer Elhauge, ‘Defining Better Monopolization Standards’ (2003) 56 *Stanford Law Review* 253; Abbott B. Lipsky and J. Gregory Sidak, ‘Essential Facilities’ (1999) 51 *Stanford Law Review* 1187.

<sup>18</sup> See e.g. James S. Venit and John J. Kallaugh, ‘Essential Facilities: A Comparative Law Approach’, in Barry E. Hawk (ed.) 1994 *Fordham Corporate Law Institute* (Kluwer Law International, 1995), which put forward that the role of the doctrine in the EU should be more limited than in the US; John Temple Lang proposes a different view in favour of the doctrine playing a more important role in the EU in ‘Defining Legitimate Competition: Companies duties to supply Competitors and Access to Essential Facilities’ collected in the same book. See also a neutral comparison between the US and EU doctrine in A Capobianco, ‘The Essential Facility Doctrine: Similarities and Differences between the American and the European Approach’, (2001) 26 *The European Law Review* 548.

the EU is *Sea Containers v Stena Sealink*<sup>19</sup>. Afterwards the definition of ‘essential facilities’ was made clear respectively in EU Commission’s notice<sup>20</sup> and General Court’s judgment in the *European Night Services* case<sup>21</sup>. The CJEU, however, like the US Supreme Court, has never formally admitted the existence of an essential facilities doctrine in the EU competition law,<sup>22</sup> even though the substance of the doctrine is argued to have been relied in many unilateral refusal cases.<sup>23</sup> Concerning refusal to license IPR in particular, the EU Commission and the Courts are less anxious to duplicate the approach applied in the tangible property cases (i.e. ports, airports and rail infrastructures) without any modification.<sup>24</sup> The essential facilities doctrine is deemed to be inadequate to address the concern at the intersection of IPR and the competition law.<sup>25</sup> Both of the Discussion Paper and the Commission Guidance support this distinction by listing *refusal to license intellectual property rights* and *refusal to grant access to an essential facility* as two forms of refusal to supply.<sup>26</sup> The approach employed in refusal to

<sup>19</sup> Case IV/34.689 *Sea Containers v Stena Sealink*, Commission Decision of 21 December 1993, [1994] OJ L15/8.

<sup>20</sup> Notice on the application of the competition rules to access agreements in the telecommunications sector, OJ 1998 C 265/2: “the expression essential facility is used to describe a facility or infrastructure which is essential for reaching customers and/or enabling competitors to carry on their business, and which cannot be replicated by any reasonable means”. (Para 68)

<sup>21</sup> Judgment of 15 September 1998, *European Night Services and Others v Commission*, T-374/94, T-375/94, T-384/94 and T-388/94, ECR, ECLI:EU:T:1998:198: “the Court considers that neither the parent undertakings nor the joint venture thus set up may be regarded as being in possession of infrastructure, products or services which are ‘necessary’ or ‘essential’ for entry to the relevant market unless such infrastructure, products or services are not ‘interchangeable’ and unless, by reason of their special characteristics - in particular the prohibitive cost of and/or time reasonably required for reproducing them - there are no viable alternatives available to potential competitors of the joint venture, which are thereby excluded from the market.” (Para 209)

<sup>22</sup> Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ (2004) 41 *Common Market Law Review* 1519, p1526. Barry Doherty, ‘Just What are Essential Facilities?’ (2001) 38 *Common Market Law Review* 397, pp.404-405.

<sup>23</sup> Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ 41 (2004) *Common Market Law Review* 1519, p1524. See also Thomas Eilmansberger, ‘The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after *IMS Health* and *Microsoft*?’ (2005) 16 *King’s College Law Journal* 329.

<sup>24</sup> Hans Henrik Lidgard, ‘Application of Article 82 EC to Abusive Exclusionary Conduct – Refusal to Supply or to License’, (2009) 4 *Europarättslig tidskrift*, 694, p707.

<sup>25</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches But No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang 2008), pp.69-70. Herbert J. Hovenkamp, Mark D. Janis and Mark A. Lemley, ‘Unilateral Refusals to License in the U.S.’ (2006) 2 *Journal of Competition Law & Economics* 1, pp.23-24.

<sup>26</sup> See *DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses*. (Hereinafter ‘Discussion Paper’), Para 209; and Communication from the Commission – *Guidance on the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by*

license cases – ‘exceptional circumstances test’<sup>27</sup>, reflects a modified and more complex essential facilities doctrine, which is the combination of the substance of essential facilities rationale plus an additional new product requirement.<sup>28</sup> Therefore, in the context of unilateral refusal cases involving IPR, as summarized by some commentators, the essential facilities doctrine is merely a useful label for a specific group of cases with common features, but does nothing to do with the analysis of the case.<sup>29</sup> Like the statements of US Supreme Court in *Trinko*,<sup>30</sup> competition liability should not invoke the essential facilities doctrine as a separate source of duties, but the arguments should be capable of undergoing a more objective and complex, economic-based analysis.<sup>31</sup>

## 2.2 Volvo: starting with a *per se* legal approach?

The legal issue of refusal to license IPR at the intersection of EU competition rules and the protection of intellectual property rights was for the first time referred to the CJEU by the national court in a car spare parts case *Volvo v. Veng*<sup>32</sup> (*‘Volvo’*). The main concern that the UK court sought to know was whether a unilateral refusal to license design rights to third parties constituted an abuse of dominant position under Article 102 TFEU. Volvo claimed that Veng had infringed Volvo’s design right on body panels by importing, manufacturing and marketing the same product without authority from Volvo.<sup>33</sup> Veng invoked Article 102 and argued that

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*dominant undertakings*, [2009] OJ C45/7 (Hereinafter ‘Commission Guidance’), Para 78.

<sup>27</sup> More discussions on the ‘exceptional circumstances test’ see below the analysis of EU case *Magill* (section 2.3), *IMS Health* (section 2.6) and *Microsoft I* (chapter 3, section 2).

<sup>28</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, p72.

<sup>29</sup> Steven Anderman, ‘The Epithet That Dares Not Speak its Name: The Essential Facilities Concept in Article 82 EC and IPRs after the Microsoft Case’, in Ariel Ezrachi (ed.) *Article 82 EC: Reflections on its Recent Evolution* (Hart Publishing, 2009), p89; John Temple Lang, ‘Defining legitimate competition: companies’ duties to supply competitors and access to essential facilities’, (1994) 18 *Fordham International Law Journal*, 437, p483; John Temple Lang, ‘The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner’ (2000) 1 *Journal of Network Industries* 375, pp.403-404; Allen Kezsbom and Alan V. Goldman, ‘No Shortcut to Antitrust Analysis: the Twisted Journey of the “Essential Facilities” Doctrine’, (1996) 1 *Columbia Business Review* 1, p1; Barry Doherty, ‘Just What are Essential Facilities?’ (2001) 38 *Common Market Law Review* 397, pp.404-405.

<sup>30</sup> *Trinko* 540 U.S. 398, 411.

<sup>31</sup> Barry Doherty, ‘Just What are Essential Facilities?’ (2001) 38 *Common Market Law Review* 397, pp.404-405.

<sup>32</sup> Judgment in *Volvo* ECLI:EU:C:1988:477. More analysis of the car spare parts cases on the intersection of EU competition rules and enforcement of intellectual property rights see e.g. Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), pp.229-267

<sup>33</sup> Judgment in *Volvo* ECLI:EU:C:1988:477, Para 3.

Volvo's refusal amounted to an abuse of its dominant position.<sup>34</sup> The Court took a strong stance for the enforcement of intellectual property rights in the form of refusal to grant a licence by stating that:

“It must also be emphasized that the right of the proprietor of a protected design to prevent third parties from manufacturing and selling or importing, without its consent, products incorporating the design constitutes the very subject-matter of his exclusive right. It follows that an obligation imposed upon the proprietor of a protected design to grant to third parties, even in return for a reasonable royalty, a licence for the supply of products incorporating the design would lead to the proprietor thereof being deprived of the substance of his exclusive right, and that a refusal to grant such a licence cannot in itself constitute an abuse of a dominant position.”<sup>35</sup>

Thus, the Court accepted that intellectual property owner's refusal to license was not a *per se* illegal practice. Without the appearance of an additional abusive element,<sup>36</sup> a pure refusal to license a protected design right to third parties would be immune from the competition liability. What is more, the behaviour of refusal to license even became a strong *per se* legal practice as the Court enumerated three examples as exceptional abusive situations in refusal cases, which were vulnerable to criticism however, as follows:

“It must however be noted that the exercise of an exclusive right by the proprietor of a registered design in respect of car body panels may be prohibited by Article [102] if it involves, on the part of an undertaking holding a dominant position, certain abusive conduct such as the arbitrary refusal to supply spare parts to independent repairers, the fixing of prices for spare parts at an unfair level or a decision no longer to produce spare parts for a particular model even though many cars of that model are still in circulation, provided that such conduct is liable to affect trade between Member States.”<sup>37</sup>

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<sup>34</sup> *ibid*, Opinion of Advocate General Mischo, Para 2.

<sup>35</sup> Judgment in *Volvo* ECLI:EU:C:1988:477, Para 8.

<sup>36</sup> On the need for an additional abusive element see for instance Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), p112; John Temple Lang, ‘Anticompetitive Non-Pricing Abuses under European and National Antitrust Law’, in Barry Hawk (ed.) *International Antitrust Law & Policy: Fordham Corporate Law 2003* (Juris Publishing, 2004) 235, pp.292-298; John Temple Lang, ‘Mandating Access: the Principles and the Problems in Intellectual Property and Competition Policy’, (2004) 15(5) *European Business Law Review* 1087, pp.1101-1103.

<sup>37</sup> Judgment in *Volvo* ECLI:EU:C:1988:477, Para 9. In judgment in *CICCA and Maxicar v Renault*, 53/87, ECLI:EU:C:1988:472, the European Court of Justice reached a similar conclusion: “It should be noted at the outset that the mere fact of securing the benefit of an exclusive right granted by law, the effect of which is to enable the manufacture and sale of protected products by unauthorized third parties to be prevented, cannot be regarded as an

It is apparent that these examples contribute little to identifying the abusive refusal behaviour on the following grounds that, firstly, the wordings used in all of the three examples are vague, resulting in that the Member States' courts would have confronted practical problems when applying these examples if they had stayed valid. In contrast with legitimate refusal behaviour in most cases, the Court did not specify what additional factor would make refusal behaviour to be *arbitrary*; in the *unfair prices* example, it is difficult, if not impossible, to set up a model to examine whether the prices fixed are fair or not, particularly when taking into account the proportionate reward for the innovative efforts of the right owner; in the last example, terminating production of spare parts for older cars is understandable in the car industry on the one hand, on the other hand the word *many* is indeed an ambiguous word that could not help the courts in Member States to find a prematurely terminating abuse without any calculating model.<sup>38</sup> Secondly, what makes refusal to license in *Volvo* judgment a *per se* legal practice rather than a legitimate practice in principle equipped with several exceptions lies in that these abusive situations listed are not examples directing at refusal to share design rights. In the first abusive example it is clear that the judgment forbade the arbitrary refusal to supply independent repairers spare parts incorporating design rights, but not the behaviour of refusal to grant independent repairers a licence to manufacture by themselves the spare parts covered by design rights.<sup>39</sup> The third example, more or less similar to the first one, was about termination of the right owner's production of the spare parts rather than termination of a license granted to independent repairers. The fixing unfair prices example was more likely to be regulated under Article 102(a) as another form of abuse of dominant position, in which the supply would be made conditional upon the acceptance of the unfair trading conditions imposed. Taking a step back, if this example could be identified as abusive refusal to deal, the unfair prices was set for supplying the spare parts produced by the right owner himself, but not the price for the license of design rights.

It has been observed that, as the starting case involving refusal to license issue, the adoption of such a *per se* legal approach was due to the fact that the Court did not manage to incorporate the

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abusive method of eliminating competition. Exercise of the exclusive right may be prohibited by Article 86 if it gives rise to certain abusive conduct on the part of an undertaking occupying a dominant position such as an arbitrary refusal to deliver spare parts to independent repairers, the fixing of prices for spare parts at an unfair level or a decision no longer to produce spare parts for a particular model even though many cars of that model remain in circulation, provided that such conduct is liable to affect trade between Member States." (Para 15-16)

<sup>38</sup> More analysis on the vagueness of these examples in *Volvo* could see Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell, 1996), pp.256, 258-261.

<sup>39</sup> *ibid*, pp.255-256.

specific anti-competitive circumstances of the case into the evaluation, failure of which resulted in its difference with the (gradually) weak *per se* legal approach adopted in the subsequent cases.<sup>40</sup>

### 2.3 The ‘exceptional circumstances test’

The *Magill* case<sup>41</sup> confirmed the main ruling in *Volvo* that “refusal to grant a licence, even if it is the act of an undertaking holding a dominant position, cannot in itself constitute abuse of a dominant position”; however, “the exercise of an exclusive right by the proprietor may involve abusive conduct in exceptional circumstances”.<sup>42</sup> The Court of Justice made *Magill* a milestone refusal to license case in the history of EU competition law by equipping the ‘exceptional circumstances test’ with four practical prongs, which made it a more concrete and workable approach.

In *Magill*, three TV companies RTE, BBC and IBA respectively had statutory monopoly on TV broadcasting in Ireland and UK, hence owned the copyright protection on their programme information.<sup>43</sup> RTE, BBC and ITP each published a weekly TV guide, offering detailed programme information of the week ahead to the households. Magill, an Irish publisher, in a very short period published a comprehensive weekly TV guide, from which the TV viewers could obtain all the programmes information available in Ireland and Northern Ireland. It offered the consumers another option; otherwise they had to buy several TV guides to obtain all programmes information. This publication was stopped by the copyright holders who obtained injunctions from national courts.<sup>44</sup> Magill complained to the EU Commission and alleged that the TV companies had abused their dominant position by refusing to license their copyrights. The Commission held that the conduct of the TV companies had infringed competition rules by wrongly exercising their IPR.<sup>45</sup>

The General Court and the Court of Justice upheld EU Commission’s decision. The Court of Justice based its judgment upon four reasons: (1) the TV companies “were, by force of circumstance, the only sources of the basic information on programme scheduling which is

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<sup>40</sup> *ibid*, pp.253-254.

<sup>41</sup> Judgment in *Magill* ECLI:EU:C:1995:98. Overview of this case see Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), pp.135-150.

<sup>42</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 49-50.

<sup>43</sup> The copyright of the IBA channels was owned by the Independent Television Publications (ITP).

<sup>44</sup> For more detailed facts see Case IV/31.851 – *Magill TV Guide / ITP, BBC and RTE*, Commission Decision of 21 Dec 1988, OJ L 78, pp.43-51, Para 1-18.

<sup>45</sup> *ibid*, Para 23.

the indispensable raw material for compiling a weekly television guide” and there was “no actual or potential substitute for a weekly television guide offering information on the programmers for the week ahead”<sup>46</sup>; (2) for the comprehensive weekly TV guide offered by Magill, “there was a specific, constant and regular potential demand on the part of consumers”<sup>47</sup>; (3) “there was no justification” on the part of the copyright holders;<sup>48</sup> (4) the TV companies “reserved to themselves the secondary market of weekly television guides by excluding all competition on that market”.<sup>49</sup>

Whereas it is illustrated that the *Volvo* case and the *Magill* case share some important similarities, the ECJ did not explain in the latter case why Article 102 TFEU may apply to refusal to license IPR but not to the refusal to sell IPR protected products.<sup>50</sup> The four conditions above constitute the four prongs of the ‘exceptional circumstances test’, with which whether the refusal conduct by a dominant undertaking is abusive or not could be assessed. This test, equipped with four conditions, is indeed a great progress compared to the strong *per se* legal rule with three exceptional abusive examples in previous spare parts cases. Yet, *Magill* test is an approach with many problems unsolved. By adopting this unpredictable ‘exceptional circumstances’ approach, it is held that the ECJ has “set a dangerous precedent for the future” and offered not much legal certainty, not only for copyright owners but also for intellectual property rights owners as a whole.<sup>51</sup> A far-reaching innovation brought about by *Magill* is the introduction of the ‘new product condition’.<sup>52</sup> Afterwards it has been confirmed in *IMS Health* and extensively interpreted in *Microsoft* thereby has invoked much debate.<sup>53</sup> Extra attention should be paid on another fact that in this case, besides the TV companies’ own use, the programme information was also licensed to the press under strict licensing conditions.<sup>54</sup> This implies that there was a market for licensing the TV programme information. What if the TV companies had not licensed to anyone besides their own use? The question of whether the evaluation of a potentially abusive refusal has something to do with the fact that IPR at stake

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<sup>46</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 52-53.

<sup>47</sup> *ibid*, Para 52.

<sup>48</sup> *ibid*, Para 55.

<sup>49</sup> *ibid*, Para 56.

<sup>50</sup> See Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), pp.146, 148.

<sup>51</sup> *ibid*, p149.

<sup>52</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 52-54.

<sup>53</sup> More discussion on the new product condition see chapter 3, section 2.3.

<sup>54</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 9.

has been marketed or not will be tackled in *IMS Health*<sup>55</sup>.

## 2.4 Cumulative or severable conditions?

The Court of Justice did not answer the question of whether the conditions in *Magill* test were cumulative or not, resulting in divergent understanding between the General Court in *Ladbroke*<sup>56</sup> and the Court of Justice in *IMS Health*. Ladbroke, who ran betting shops in Belgium and took bets on horse races, complained to the Commission claiming that the French race course operator had abused its dominant position by refusing to license the copyright of the televised pictures and sound commentaries.<sup>57</sup> The Commission maintained that the exceptional circumstances were not present in this case and rejected the complaint, which afterwards was supported by the General Court. The Court surprisingly held that the ‘new product condition’ and the ‘indispensability condition’ were alternative rather than cumulative:

“The refusal to supply the applicant could not fall within the prohibition laid down by Article [102] unless it concerned a product or service which was either essential for the exercise of the activity in question, in that there was no real or potential substitute, *or* was a new product whose introduction might be prevented, despite specific, constant and regular potential demand on the part of consumers.”<sup>58</sup>

On the one hand, after analyzing the relation between televised broadcasting and the main activities of betting companies, the Court found that the former was not essential or indispensable for the latter;<sup>59</sup> on the other hand, it is clear that the refusal in question did not prevent the emergence of any new product in this case. According to this *alternative conditions* interpretation, refusal to license would infringe Article 102 TFEU either when the intellectual property requested is indispensable for the downstream market, or the appearance of a new product has been hindered.

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<sup>55</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257.

<sup>56</sup> Judgment of 12 June 1997, *Tierce Ladbroke SA v Commission*, T-504/93, ECR, ECLI:EU:T:1997:84.

<sup>57</sup> *ibid*, Para 1-9.

<sup>58</sup> *ibid*, Para 131. (emphasis added)

<sup>59</sup> *ibid*, Para 132. (“[T]he televised broadcasting of horse races, although constituting an additional, and indeed suitable, service for bettors, it is not in itself indispensable for the exercise of bookmakers’ main activity, namely the taking of bets, as is evidenced by the fact that the applicant is present on the Belgian betting market and occupies a significant position as regards bets on French races. Moreover, transmission is not indispensable, since it takes place after bets are placed, with the result that its absence does not in itself affect the choices made by bettors and, accordingly, cannot prevent bookmakers from pursuing their business.”)



## 2.5 What does indispensability mean?

*Oscar Bronner*<sup>60</sup>, a case about refusing third parties to access its nation-wide newspaper delivery network, is a leading case on the definition of *indispensability* even though IPR was not involved in this case. To establish that the intellectual property requested is indispensable for the competitors on the downstream market, it should not only be undisputed that there is no other available substitutes, even though they may be disadvantageous,<sup>61</sup> but it should also be demonstrated that there are “technical, legal or even economic obstacles capable of making it impossible, or even unreasonably difficult, for any other undertaking alone or in cooperation to potentially establish a substitute”.<sup>62</sup> Furthermore, the Court of Justice emphasised that such kind of impossibility, or unreasonably difficulty, should be measured from the perspective of an *as efficient competitor*, but not necessarily from the perspective of the requesting parties.<sup>63</sup>

## 2.6 Modification of the ‘exceptional circumstances test’ by *IMS Health*

*IMS Health*<sup>64</sup> is the latest one which further modified the ‘exceptional circumstances test’ before *Microsoft I*. IMS was the world leader undertaking of collecting information on sales and prescriptions of pharmaceutical products. With the assistance of its customers—the pharmaceutical companies, IMS developed a ‘1860 brick structure’ to present such data in German market by dividing the German market into 1860 zones according to postcodes and this product subsequently became the *de facto* industry standard. When NDC offered an alternative product – ‘3000 brick structure’ on the same market, IMS relied on its copyright and sued NDC to German court.<sup>65</sup> The Landgericht in Frankfurt granted an order prohibiting NDC to continue using the ‘3000 brick structure’ considering that NDC’s product was derived from IMS’s ‘1860 brick structure’ which as a database was under copyright protection. NDC asked for a license but was refused by IMS. NDC complained to the EU Commission, claiming that IMS’s refusal was an abuse of its dominant position. On the one hand, the Commission issued an interim decision requiring IMS to license its copyright to NDC,<sup>66</sup> which was afterwards suspended by an order from the General Court;<sup>67</sup> on the other hand, national copyright proceedings continued in German courts and a reference to the Court of Justice was made by the Frankfurt

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<sup>60</sup> Judgment in *Oscar Bronner* ECLI:EU:C:1998:264.

<sup>61</sup> *ibid*, Para 43.

<sup>62</sup> *ibid*, Para 44.

<sup>63</sup> *ibid*, Para 45-46. See also Opinion of Advocate General Jacobs, Para 68.

<sup>64</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257.

<sup>65</sup> *ibid*, Para 3-8.

<sup>66</sup> Case COMP D3/38.044, *NDC Health v IMS Health*, Commission Decision of 3 July 2001, [2002] OJ L59/18.

<sup>67</sup> Judgment of 26 October 2001, *IMS Health v Commission*, T-184/01 R, ECR, ECLI:EU:T:2001:259, Order of the President of the General Court.

Landgericht.

On the one hand, the Court of Justice confirmed the ‘exceptional circumstances test’ established in *Magill*. Contrary to the viewpoint of the General Court in *Ladbroke*, the Court made it clear that the conditions should be applied *cumulatively*.<sup>68</sup> On the other hand, the court implied that other circumstances might also be capable of justifying a compulsory license, by alleging that the conditions in *Magill* test were “sufficient” rather than “necessary”.<sup>69</sup>

The Court restated the view in *Bronner* that, to establish indispensability, it has to be examined whether alternative solutions exist, even they might be more expensive or technologically not so advanced as the product or service concerned.<sup>70</sup> Exercise of copyrights, compared to patents, rarely conflicts with competition rules since copyrights are designed to protect a particular expression of an idea rather than the idea itself.<sup>71</sup> *Magill* and *IMS Health* have been identified as exceptions because either the copyright holder was the unique source of information requested, or the copyrighted product became a *de facto* standard in the industry. Leaving the question of whether such IPR as input was indispensable to the national court to decide, the Court of Justice suggested that “a high level of participation by the pharmaceutical laboratories in the improvement of the 1860 structure” must be taken into account.<sup>72</sup> It was believed that the customer participation made them afterwards rely on the ‘1860 brick structure’ and therefore switching to alternative products would cause “exceptional organisational and financial efforts”.<sup>73</sup> However, customer preference itself was not enough to make the brick structure indispensable because the competitors were still capable of entering into the market by providing alternative products to the customers.<sup>74</sup> In this respect, it should firstly figure out whether it was the participation of the major customers that contributed to the *de facto* standard, or the customers had no choice but to choose the brick structure in question after ‘1860 brick structure’ had become the *de facto* standard. Apparently *IMS* case belongs to the former case.

With regard to the new product condition, the Court of Justice maintained that the protection of

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<sup>68</sup> See e.g. Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 38 and 52.

<sup>69</sup> *ibid*, Para 38.

<sup>70</sup> *ibid*, Para 28.

<sup>71</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, fn 65.

<sup>72</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 29.

<sup>73</sup> *ibid*.

<sup>74</sup> See R O’Donoghue and J Padilla, *The Law and Economics of Article 82* (Hart Publishing, 2006), p442.

free competition prevails over the protection of IPR and the right holder's contractual freedom only if the refusal has resulted in prevention of the development of the downstream market and such anti-competitive effect would pass onto the consumers.<sup>75</sup> Although prevention of a new product provided by the competitors on the downstream market was considered as the only proxy to evaluate whether the competition of the downstream market has been distorted to the detriment of consumers, other circumstances might also suffice to decide in balancing between the interest of IPR holder and the interest of the competitive process, whilst taking into consideration that, as mentioned before, the Court regarded these conditions were *sufficient* rather than *necessary*. Regarding the exact meaning of a new product, the Court neither answered the question of how to evaluate the novelty of a new product, nor specified the way to measure a potential consumer demand, only stating that:

“the refusal ... may be regarded as abusive only where the undertaking which requested the licence does not intend to limit itself essentially to duplicating the goods or services already offered on the secondary market by the owner of the intellectual property right, but intends to produce new goods or services not offered by the owner of the right and for which there is a potential consumer demand.”<sup>76</sup>

With respect to the condition of likelihood of excluding all competition on the downstream market, the judgment confirmed the necessity of involvement of two neighbouring markets.<sup>77</sup> Whether the products on the upstream and downstream markets were marketed, according to the Court, was irrelevant. By referring to the *Bronner* case, the Court concluded that the fact that the product was “not marketed separately would not preclude the possibility of identifying a separate market”.<sup>78</sup> Furthermore, it is sufficient if “a potential market or hypothetical market can be identified”.<sup>79</sup> In other words, the existence of two production stages is sufficient in the sense that the product or service on the primary stage is indispensable for the production on the subsequent production stage.<sup>80</sup> Therefore, even the TV companies had not licensed their programme information to some presses in *Magill*, a same conclusion would be reached, because according to the Court's view in *IMS Health* whether there existed a licensing market of the IPR in question is irrelevant to identifying a separate market. The Court did not give any

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<sup>75</sup> See Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 27, Para 48. See also Opinion of Advocate General Tizzano, Para 62.

<sup>76</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 49.

<sup>77</sup> *ibid*, Para 44.

<sup>78</sup> *ibid*, Para 40-43.

<sup>79</sup> *ibid*, Para 44.

<sup>80</sup> *ibid*, Para 45.

guidance to IPR holders on how to justify the refusal and left it to the national courts.<sup>81</sup>

### 3. The modernisation of Article 102 TFEU: from the *Discussion Paper* to the *Commission Guidance*

The Modernisation of the enforcement of Article 102 TFEU started in 2005. In that year the EU Commission published a Commission Discussion paper on the application of Article 102 TFEU to exclusionary abuses, which welcomed comments from the public.<sup>82</sup> It appears to summarize and elaborate the evolving experience of the Commission, as well as that of the Court of Justice, with the application of Article 102 TFEU.<sup>83</sup> The Discussion Paper, according to former Competition Commissioner Neelie Kroes, did not intend to “propose a radical shift in enforcement policy”, but to explain how theories of harm should, following a more economic-based approach, be applied in the most frequent types of abusive practices.<sup>84</sup>

The Discussion Paper has a full section on refusal to license IPR. However, it is unclear why the issue is only dealt with in the section of *refusal to start supplying an input*, but not in the section of *termination of an existing supply relationship*. This arrangement conflicts with the Commission’s experience in *Microsoft*, which has demonstrated that Article 102 TFEU also applies to the refusal to continue licensing the IPR requested.

To justify an order of compulsory license, the Discussion Paper concludes that following conditions shall be fulfilled: (1) “the behaviour can be properly characterized”; (2) “the refusing undertaking is dominant”; (3) “the input is indispensable”; (4) “the refusal is likely to have a negative effect on competition”; (5) “the refusal is not objectively justified”;<sup>85</sup> (6) the refusal prevents the emergence of new goods or services not offered by the IPR owner for which is a potential consumer demand.<sup>86</sup> As the Court of Justice implied in *IMS Health* that

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<sup>81</sup> *ibid*, Para 51.

<sup>82</sup> Discussion Paper, *supra* note 26.

<sup>83</sup> *ibid*, Para 5.

<sup>84</sup> Neelie Kroes, ‘Preliminary thoughts on policy review of Article 82’, speech at *Fordham Corporate Law Institute*, New York, 23 September 2005, SPEECH/05/537. Available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/05/537&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 6 Dec 2011.

<sup>85</sup> These five conditions are provided in ‘9.2.2 refusal to start supplying an input’ and elaborated from 9.2.2.1 to 9.2.2.5 of Discussion Paper, *supra* note 26.

<sup>86</sup> See Discussion Paper, *supra* note 26, Para 239.

these cumulative conditions might be not exhaustive,<sup>87</sup> the Discussion Paper also hints that these conditions might be *examples*, rather than an exhaustive list of the exceptional circumstances.<sup>88</sup>

The description of these conditions provoked various criticisms, which claim that the Discussion Paper deviated from the case law in some important respects.<sup>89</sup> Concerning the condition of the likelihood of excluding all competition on the downstream market, the Discussion Paper proposes that a “likely negative effect on competition” shall suffice.<sup>90</sup> It turns to emphasis the likely effect on the market by the refusal. The elimination of all competition is not necessarily required. In some cases even the exclusion of one particular competitor could justify the intervention of public power, if such exclusion has a significant impact because of the competitor’s important identity.<sup>91</sup>

With respect to the new product condition, the Discussion Paper, on the one hand, almost repeats the wording in the judgment of *IMS Health* case.<sup>92</sup> However, on the other hand, according to the Discussion Paper, “a refusal to license an IPR protected technology which is indispensable as a basis for *follow-on innovation* by competitors may be abusive even if the license is not sought to directly incorporate the technology in clearly identifiable new goods and services”.<sup>93</sup> Thus, the Discussion Paper has adopted a lower criterion for technology market without explicitly explaining the economic basis for such a broad presumption in favour of follow-on innovations.<sup>94</sup> Abandonment of the original narrow interpretation of the new product condition not just makes the assessment of this condition legally uncertain, but also

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<sup>87</sup> See Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 48. See also Opinion of Advocate General Tizzano, Para 62.

<sup>88</sup> See Discussion Paper, *supra* note 26, Para 239.

<sup>89</sup> See e.g. Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, pp.82-89.

<sup>90</sup> Discussion Paper, *supra* note 26, Para 231-232.

<sup>91</sup> *ibid.*

<sup>92</sup> *ibid.*, Para 239. (“The refusal to grant a license prevents the development of the market for which the license is an indispensable input, to the detriment of consumers. This may only be the case if the undertaking which requests the license does not intend to limit itself essentially to duplicating the goods or services already offered on this market by the owner of the IPRs, but intends to produce new goods or services not offered by the owner of the right and for which there is a potential consumer demand.”)

<sup>93</sup> *ibid.*, Para 240. (emphasis added)

<sup>94</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, p86.

weakens the indispensability test.<sup>95</sup> Evidently, to prove that the IPR at stake is indispensable for follow-on innovations would be much easier for competition authorities or the requesting parties.

Concerning the possible defences upon which a dominant undertakings could rely, firstly it is worth noting that the Discussion Paper proposes to broaden the system that may escape the dominant undertaking from the prohibition of Article 102 TFEU, by introducing the concept of ‘efficiency defence’<sup>96</sup>, which is also applicable in refusal to license in particular.<sup>97</sup> The dominant undertaking in question could demonstrate that the positive effects of the refusal outweigh the negative effects on the competition process if following conditions could be proved: (1) as a result of the refusal conduct, the efficiencies are realised, or likely to be realised; (2) the refusal concerned is indispensable to realise the efficiencies; (3) the efficiencies are beneficial to consumers; (4) the competition in the downstream market is not eliminated.<sup>98</sup> Secondly, the Discussion Paper shifts the burden of proving justifications and efficiencies onto the dominant undertaking.<sup>99</sup> It has been criticized that such a shift of burden of proof has deviated from the *one-step* analysis in case law, which includes the consideration of objective justifications into the finding of abuse, into a *two-step* analysis where a defence could be claimed by the dominant undertaking after a *prima facie* infringement has been found.<sup>100</sup> With respect to refusal to license cases in particular, it is the dominant undertaking’s task to show a superior interest in protecting the incentive of the IPR holder to invest and innovate before the Commission weighs the positive and negative effects of ordering a compulsory license.<sup>101</sup> It appears that the Discussion Paper has fundamentally re-defined the role played by the Commission. The new arrangement of burden of proof would result in a “full-fledged cost-benefit analysis”, leaving the Commission with broad discretion without limiting principles.<sup>102</sup> A balancing of possible effects on innovation and competition, requiring

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<sup>95</sup> *ibid.*

<sup>96</sup> Discussion Paper, *supra* note 26, Para 77, 79, and 84-92.

<sup>97</sup> *ibid.*, Para 235-236.

<sup>98</sup> *ibid.*, Para 84.

<sup>99</sup> *ibid.*, Para 77.

<sup>100</sup> See Alvertina Albors-Llorens, ‘The Role of Objective Justification and Efficiencies in the Application of Article 82 EC’ (2007) 44 *Common Market Law Review* 1727, pp.1754-1755; Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, pp.86-87.

<sup>101</sup> Discussion Paper, *supra* note 26, Para 236.

<sup>102</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and*

sufficient information of the relevant markets and reasonable prediction of future development of these markets, would be a formidable task for the Commission and might result in a number of errors of false intervention, especially in some industries characterized by network effects.<sup>103</sup>

On 3 December 2008, the European Commission published its comprehensive guideline to the business community and competition law enforcers at the level of Member States on the Commission's enforcement priorities in applying Article 102 TFEU to abusive exclusive conduct by dominant undertakings.<sup>104</sup> An economic and effects-based approach, which has been regarded at the heart of Article 102 modernisation since former Commissioner Monti,<sup>105</sup> has been formally adopted by the Commission Guidance.<sup>106</sup> While the analytical framework in the Commission Guidance is argued to be “hardly revolutionary” but just “a statement of the obvious” – in other words the economic and effects-based approach is not yet fully-fledged – the modernisation nevertheless, generally speaking, has brought the assessment of potential abusive exclusionary practise to a large extent in keeping with the control of anti-competitive agreements and merger cases.<sup>107</sup>

In the part of analysis frameworks for specific forms of exclusionary abuses, the Commission Guidance, unlike the Discussion Paper, neither distinguishes between refusal to license IPR and refusal to supply other properties, nor applies different attitudes towards previous existing

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*the Public Interest* (P.I.E. Peter Lang, 2008) 59, p84, 86.

<sup>103</sup> *ibid*, pp.87-88.

<sup>104</sup> Commission Guidance, *supra* note 26.

<sup>105</sup> See e.g. the foreword by Mario Monti in *European Commission XXXth Report on Competition Policy 2000*, Brussels-Luxembourg, 2001, available at [http://ec.europa.eu/competition/publications/annual\\_report/2000/en.pdf](http://ec.europa.eu/competition/publications/annual_report/2000/en.pdf) , last visited on 27 Feb 2013, “[t]he ongoing process of updating our rules and procedures is driven by the need to strengthen the enforcement of EC competition law throughout the European Union. We believe that this final objective requires a simplification of procedures, a *more economic approach* to the analysis of cases, a greater involvement of national competition authorities and national courts in the application of EU competition law.” (p9, emphasis added)

<sup>106</sup> See Commission press release IP/08/1877 of December 3, 2008, ‘Antitrust: consumer welfare at heart of Commission fight against abuses by dominant undertakings’, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/1877&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 6 Dec 2011. According to the press release, such an approach has been already used in several cases prior to this Commission Guidance.

<sup>107</sup> Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p929. See also Manuel Kellerbauer, ‘The Commission's new enforcement priorities in applying article 82 EC to dominant companies' exclusionary conduct: A shift towards a more economic approach?’, (2010) 31(5) *European Competition Law Review* 175, p183.

customers and new customers.<sup>108</sup> The Commission Guidance starts with the general rule which has been confirmed a couple of times since the spare parts cases, that a dominant undertaking should have the right to independently handle its property and feel free to choose its business partners.<sup>109</sup> The imposition of an obligation to license IPR on the dominant undertaking would be taken into consideration by the Commission only in the case where three cumulative conditions are fulfilled: (1) “the refusal relates to a product or service that is objectively necessary to be able to compete effectively on a downstream market” (indispensability); (2) “the refusal is likely to lead to the elimination of effective competition on the downstream market” (elimination of competition); (3) “the refusal is likely to lead to consumer harm” (consumer harm).<sup>110</sup> It is worth noting that the third condition has departed from EU case law in the sense that the condition of prevention of a new product in *Magill/IMS Health*, or the condition of hindrance of technological development in *Microsoft*,<sup>111</sup> has been replaced by a broader consumer harm test which evaluates likely negative consequences on the consumers brought about by the refusal. The prevention of a new product, disregarding in which way it is interpreted (narrowly or extensively), has been no longer a separate prong in the ‘exceptional circumstances test’, but merely as the main indicative factor in evaluating likely consumer harm to raise the concern of the Commission to pursue the refusal behaviour.<sup>112</sup> If these conditions are cumulatively met, the dominant undertaking concerned may justify its refusal by invoking objective necessity or efficiencies defence.<sup>113</sup> ‘Meeting competition defence’ is apparently not an acceptable plea in the Guidance.<sup>114</sup> A dominant undertaking, according to the Commission Guidance, may justify its conduct by demonstrating that the purpose of its refusal is to obtain sufficient profit on the investment or to keep its innovation from being

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<sup>108</sup> Commission Guidance, *supra* note 26, Para 78.

<sup>109</sup> *ibid*, Para 75.

<sup>110</sup> *ibid*, Para 81, 83-88.

<sup>111</sup> Detailed analysis of EU *Microsoft I* case see chapter 3.

<sup>112</sup> Anne C. Witt has concluded, from a general perspective though, that the analytical approach in the Commission Guidance that requires direct consumer harm to be necessary for an abuse appears not compatible with the case law in her contribution ‘The Commission’s Guidance Paper on Abusive Exclusionary Conduct – More radical than it appears?’, (2010) 35 *European Law Review* 214, pp.223-225.

<sup>113</sup> For detailed procedural provisions about evidence summing, see Commission Notice on Best Practices for the Conduct of Proceedings Concerning Article 101 and 102 TFEU, [2011] OJ C-308/06; see also DG Competition staff working paper Best Practices for the Submission of Economic Evidence and Data Collection in Cases Concerning the Application of Article 101 and 102 TFEU and in Merger Cases, available at [http://ec.europa.eu/competition/antitrust/legislation/best\\_practices\\_submission\\_en.pdf](http://ec.europa.eu/competition/antitrust/legislation/best_practices_submission_en.pdf), last visited on 4 Dec 2011.

<sup>114</sup> Analysis on the (in)applicability of the ‘meeting competition defence’ in refusal to license cases see *infra* chapter 3, section 2.4.2.



unfavourably impaired.<sup>115</sup> To determine whether or not to pursue the case, the Commission would put the benefits and costs of a compulsory license – the former being the introduction of new/innovative products or technological development, the latter being the incentive of the dominant undertaking to invest and innovate – on the scale.<sup>116</sup> In other words, the Commission has to decide whether the dynamic efficiency prevails over the static efficiency, or *vice versa*. It is argued that this balancing approach has deviated from a “weak *per se* lawful rule” developed in the fundamental case law towards a “rule of reason analysis”.<sup>117</sup>

## **4. Preliminary issues on relevant markets and dominance**

The substance of abusive refusal to license is that, by the conduct of refusal, a dominant undertaking leverages its market power from one market onto the other, and thereby eliminates the competition on the latter market to the detriment of consumers. Accordingly, prior to examining whether there is an abuse, the competition authorities and the courts need to ensure that: (1) there are two adjacent and separate markets; (2) the dominant undertaking is dominant on one market from which the market power could be leveraged onto another market. Whether the refusal has left the other market to the dominant undertaking itself is not a preliminary issue, but is nonetheless a concern to be addressed by the ‘exceptional circumstances test’.

### **4.1 Defining relevant market in refusal to license cases**

#### **4.1.1 Narrower product market against wider geographic market**

Defining relevant product market in Article 102 TFEU cases involving IPR needs to be cautiously contemplated because any conceivable technique, including SSNIP test, is claimed to be incompetent.<sup>118</sup> For IPR holders, the determination of the relevant product at issue, upon which the relevant market is based, may be an even more important preliminary step. The more technically complex a product is, the greater discretion of the competition authorities would be involved to define the relevant market. This is typical in the ‘dynamically competitive industries’.<sup>119</sup> Though the products might be recognised substitutable from the perspective of consumers, the difference between each product in those industries could be evident, resulting

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<sup>115</sup> See Commission Guidance, *supra* note 26, Para 89.

<sup>116</sup> Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p903.

<sup>117</sup> *ibid*, p903.

<sup>118</sup> See Discussion Paper, *supra* note 26, Para 13.

<sup>119</sup> See *infra* section 5.2.2 for more discussion on ‘dynamically competitive industries’.

in that the relevant market is defined too narrowly.<sup>120</sup> This is particularly the case if potential competitive constraints have been ignored, just as the Discussion Paper did.<sup>121</sup> The Commission has been contested for adopting a narrow market definition.<sup>122</sup> Once a narrower relevant market has been established, the IPR holder would face a domino effect. In the first place, the narrow definition of product will reduce the possibilities of finding its substitutions, which in turn would give rise to a narrower product market or even a single product market. Secondly, the finding of a narrower product market, or a single product market, tends to discover a strong market power, or even dominance to the point of constituting a *de facto* monopoly.<sup>123</sup>

Speaking of defining relevant geographic market, given the fact that IP laws – at least copyright law and patent law – have not been harmonised at EU level, its characteristic of territoriality may lead to a narrow definition of geographic market by the EU Commission. However, by virtue of the economic globalization it is not possible to limit the marketing of IPR products any longer in the area where the exclusive rights derive from. Taking into account of other factors, such as the further integration of the European internal market and the expansion of the Internet, it shall be drawn that relevant geographic market might be expanded to an EU level or even global level. Take the *Intel* case<sup>124</sup> for example, the Commission defined a worldwide geographic market as a consequence of that “the main supplies compete globally, CPU architectures are the same around the world, the main customers (OEMs) operate on a worldwide basis, and the cost of shipping CPUs around the world is compared to their cost of manufacture”.<sup>125</sup>

#### **4.1.2 Two markets requirement**

Normally there is no obligation on the dominant firm to help his competitors in the same relevant market by granting access to his essential IPR, which is the essence of IPR

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<sup>120</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’ available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, p25.

<sup>121</sup> *ibid.*

<sup>122</sup> Alison Jones and Brenda Sufrin, *EC Competition Law: text, cases, and materials* (second edition, Oxford University Press, 2007), p299.

<sup>123</sup> Steven Anderman and Hedvig Schmidt, *EU competition law and intellectual property rights: the regulation of innovation* (second edition, Oxford University Press, 2011), p45.

<sup>124</sup> Case COMP/C-3/37.990-Intel, Commission Decision of 13 May 2009.

<sup>125</sup> *ibid.*, Para 836.

protection.<sup>126</sup> It is pro-competitive to encourage the market participants to compete on the merits, in other words, to allow undertakings to develop and keep their own advantages.<sup>127</sup> The dominant undertaking would not be expected to take responsibility for the less appealingness of the competitors' products to consumers unless the incumbent's conduct, refusal to license for instance, has made his competitors' products "positively less attractive or less readily available than they would otherwise be".<sup>128</sup> Such an obligation could only be imposed when there are two neighbouring markets involved.<sup>129</sup> A compulsory license is usually more likely with the increase of the distinction between the two markets and the anti-competitive effect on the second market due to the refusal.<sup>130</sup>

The Commission found two separate markets in *Magill*, namely the market for TV listings information and the market for weekly TV guides. The *IMS Health* judgment confirmed the necessity of the establishment of two markets as the basis of application of the 'exceptional circumstances test'.<sup>131</sup> The Court explored the question of whether it was necessary that the products on both of two markets were marketed. By referring to the *Bronner* case, the Court concluded that the fact that the product was "not marketed separately would not preclude the

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<sup>126</sup> See, for instance, the CJEU put it in Case 238/87 *Volvo*: "The right of a proprietor of a protected design to prevent third parties from manufacturing and selling or importing, without his consent, products incorporating the design constitutes the very subject-matter of his exclusive right. It follows that an obligation imposed upon the proprietor of a protected design to grant to third parties, even in return for a reasonable royalty, a licence for the supply of products incorporating the design would lead to the proprietor thereof being deprived of the substance of his exclusive right, and that a refusal to grant such a licence cannot in itself constitute an abuse of a dominant position". (Para 8) See also Robert O'Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p436.

<sup>127</sup> Robert O'Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p436.

<sup>128</sup> John Temple Lang, 'Anticompetitive Non-Pricing Abuses under European and National Antitrust Law', in Barry Hawk (ed.) *International Antitrust Law & Policy: 2003 Fordham Corporate Law 2003* (Juris Publishing, 2004) 235, p243.

<sup>129</sup> See John Temple Lang, 'Anticompetitive Abuses under Article 82 involving Intellectual Property Rights', in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?* (Hart Publishing, 2006) 589, p610: "in two-market situations because a competitor in the downstream market that gains control of a necessary input is not offering a better or a cheaper product in the downstream market, but only getting power to harm consumers in that market by shutting out its competitors", "in a single market situation, something that is 'necessary' to compete can only be a competitive advantage". See also Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexel (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, p59.

<sup>130</sup> John Temple Lang, 'The Principle of Essential Facilities in European Community Competition Law – the Position since *Bronner*' (2000) 1 *Journal of Network Industries* 375, pp.389-390.

<sup>131</sup> Case C-418/01 *IMS Health*, Para 44.

possibility of identifying a separate market”.<sup>132</sup> In other words, it is sufficient that “a potential market or hypothetical market can be identified”.<sup>133</sup> Furthermore, the existence of two separate production stages is necessary in the sense that the product or service on the primary stage is indispensable for the production on the secondary stage.<sup>134</sup> These have been afterwards confirmed in the *Microsoft* case.<sup>135</sup>

These two neighbouring markets, according to Heinemaan, could be identified into two categories: vertical-related markets and conglomerate markets.<sup>136</sup> Vertical-related markets are normally those located respectively in upstream and in downstream. The products on downstream markets are closer to end consumers while the products on the upstream markets, normally as inputs for products on the downstream markets, are not directly consumed by end users and thus are not at the same level with downstream markets.<sup>137</sup> Primary-aftermarkets are another type of two vertical-related markets.<sup>138</sup> One main feature of primary-aftermarkets situation compared to the upstream-downstream markets, apart from the fact that purchase of the aftermarket product is for the sake of the overall performance of the primary market product, is that the primary market and the aftermarket are considered equally close to the final consumers.<sup>139</sup> Take *Magill* and *Volvo* as examples (see table 2 below), consumers of weekly TV guide on the downstream market might have no interest to know from whom and how the TV guide publishers get the listing information on the upstream market; on the other hand, consumers of car spare parts on the aftermarket are also the buyers of cars on the primary market.

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<sup>132</sup> *ibid*, Para 40-43.

<sup>133</sup> *ibid*, Para 44.

<sup>134</sup> *ibid*, Para 45.

<sup>135</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289: “[I]t is necessary to distinguish two markets, namely, a market constituted by that product or service and on which the undertaking refusing to supply holds a dominant position and a neighbouring market on which the product or service is used in the manufacture of another product or for the supply of another service. The fact that the indispensable product or service is not marketed separately does not exclude from the outset the possibility of identifying a separate market”. (Para 335)

<sup>136</sup> Andreas Heinemann, ‘The contestability of IP-protected markets’ in Josef Drexler (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54.

<sup>137</sup> Discussion Paper, *supra* note 26, Para 70.

<sup>138</sup> As put forward in section 10 of the Discussion Paper, *supra* note 26, ‘aftermarkets’ or ‘secondary markets’ comprise complementary products that are purchased after the purchase of products on the primary markets (Para 243). More discussion on the concept ‘aftermarket’ also see Hendrik Bourgeois, ‘How to treat aftermarkets under Article 102 TFEU’ in Inge Govaere, Reinhard Quick and Marco Bronckers (eds.), *Trade and Competition Law in the EU and Beyond* (Edward Elgar, 2011) 349.

<sup>139</sup> Discussion Paper, *supra* note 26, fn 54.

Conglomerate markets, unlike the former situations, are not vertically related. Conglomerate markets, including one central market and one or several neighbouring markets, in IPR cases are typically connected by interoperability information.<sup>140</sup> In the example of *Microsoft* case, the market for workgroup server operating systems is one of the surrounding markets, onto which Microsoft leveraged its market power from the market for client PC operating systems by rejecting the access to the interoperability information. In contrast to the case of upstream-downstream markets, both of the products on the central market and the surrounding market are directly consumed by final users; on the other hand, contrary to the case of primary-aftermarket, purchase of the product on the surrounding market is not necessarily based on the premise of purchasing the product on the central market.

Table 2

	Upstream-downstream market	Primary-after markets	conglomerate markets
Case example	<i>Magill</i>	<i>Volvo</i>	<i>Microsoft</i>
Market X	TV listing information	Car	Client PC operating system
What a dominant undertaking owns	Copyright on programme information	Design rights on spare parts	Interoperability information
Market Y	Weekly TV guide	Spare parts	Workgroup server operating system

#### 4.1.3 Potential upstream market

In *IMS Health* the Court of Justice explicitly held that a potential or hypothetical market is sufficient to be identified as a separate market.<sup>141</sup> This conclusion had, actually, been hinted to some extent in *Bronner*, where the essential input was not separately marketed. Not only may a potential market appear on the upstream, but it may also be on the downstream.<sup>142</sup> In the case of

<sup>140</sup> Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexler (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, pp.73-74

<sup>141</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 44.

<sup>142</sup> To be clear, unless otherwise specified, in the following text the terminology 'upstream market' means the market where the IPR locates, including the concepts 'upstream market', 'primary market', and 'central market' of conglomerate markets in section 5.1.2; 'downstream market' refers to the market where the IPR concerned is used as

a potential upstream market, this lower standard for the two market requirement has attracted quite a lot of criticism.

Firstly, due to the specific characteristic of IPR, if a potential upstream licensing market could suffice to establish a separate market, the two markets requirement would be automatically satisfied and thus become an empty pre-condition prior to application of the ‘exceptional circumstances test’, since theoretically any IPR could potentially be licensed and constitute an upstream licensing market.<sup>143</sup> Secondly, although an abuse does not follow from the distinction of an upstream licensing market and a downstream market, above all a clear line to distinct two markets should be drawn.<sup>144</sup> However, whether the essential input produced in the upstream production stage could constitute a separate market or merely a competitive advantage is not clear. One commentator critically interprets the judgment as saying that it is enough “even if the input is a competitive advantage of a kind which has never previously been marketed or licensed by any company, and which it would not be economically rational to license to a direct competitor”.<sup>145</sup> The concept of potential upstream licensing market implies that a competitor’s demand for access to the dominant undertaking’s technological advantage, normally the most significant competitive advantage of the dominant undertaking in dynamically competitive industries, would suffice a forced licensing, which would particularly harm the development of these innovative industries.<sup>146</sup> Hence, a dominant undertaking would be required to take

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an essential input, including the concept ‘downstream market’, ‘aftermarket’ and ‘surrounding markets’ in section 5.1.2.

<sup>143</sup> See e.g. Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ 41 (2004) *Common Market Law Review* 1519, p1530; Andreas Heinemann, ‘The contestability of IP-protected markets’ in Josef Drexl (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, pp.59-60; Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p151; John Temple Lang, ‘Anticompetitive Abuses under Article 82 involving Intellectual Property Rights’, in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?* (Hart Publishing, 2006) 589, fn 41; James Killick, ‘*IMS* and *Microsoft* Judged in the Cold Light of *IMS*’ (2004) 1(2) *The Competition Law Review* 23, pp.27-28.

<sup>144</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p437.

<sup>145</sup> John Temple Lang, ‘Anticompetitive Non-Pricing Abuses under European and National Antitrust Law’, in Barry Hawk (ed.) *International Antitrust Law & Policy: Fordham Corporate Law 2003* (Juris Publishing, 2004) 235, p307.

<sup>146</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, p45; Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches But No Way Ahead?’ in Inge

responsibility for creating robust competition in the market where it has dominant position rather than in a downstream market.<sup>147</sup> Thirdly, identifying an upstream market merely based on the existence of different production stages would make the test unpredictable. Furthermore, defining the product market narrowly by reference to separate consumer demands – especially in the case of products such as consumables and spare parts<sup>148</sup> – is one thing, but identifying the two different stages of production as two separate markets is another. In a long term, protection of the competitive environment, which is claimed to be prevailed by the EU’s pursuing of “regulatory aspirations”, would at an unfavourable position.<sup>149</sup>

Therefore, in order to identify a potential upstream market the answers to the following three questions might play a vital role: (1) Intent: whether the dominant undertaking is willing to license his IPR to the competitors, or whether there is any previous licensing or sharing agreements?<sup>150</sup> (2) Likelihood of distinguishing the production of the IP from the production of the final product: whether the IP could be clearly identified as, let us say, a separate intermediate product? (3) Separate consumer demand: whether there is separate consumer demand rather than the requests from the rivals for the IP concerned?

#### **4.1.4 Potential downstream market**

Another possibility of potential market - a potential downstream market - has rarely been

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Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, p77.

<sup>147</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p152.

<sup>148</sup> i.e. Judgment in *Hugin*, 22/78, ECLI:EU:C:1979:138; Judgment in *Hilti AG v Commission*, C-53/92 P, ECLI:EU:C:1994:77; Judgment of 6 October 1994, *Tetrapak v Commission*, T-83/91, ECR, ECLI:EU:T:1994:246; Judgment in *Renault* ECLI:EU:C:1988:472; Judgment in *Volvo* ECLI:EU:C:1988:477. See Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights* (second edition, Oxford University Press, 2011), pp.40-46.

<sup>149</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, p77.

<sup>150</sup> Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights* (second edition, Oxford University Press, 2011), pp.113-14: “[A]rticle 102 can be infringed when a company such as Microsoft with an industrial standard, limits technical development by refusing to continue to share interface information and thereby prevents competitors on related markets from developing their interoperable systems. If Microsoft had opted for a closed system in the way say of Apple Mac initially, the circumstances might have been different and it would normally have been entitled to continue to compete on that basis.”

discussed so far. The Discussion Paper briefly states that a refusal may have a negative impact on the competition in the sense that it has prevented a new product on a *new and not yet existing* market.<sup>151</sup> The ‘exceptional circumstances test’ does not cover such a situation where a potential new product may by itself create a totally new and not yet existing market.<sup>152</sup> Put another way, is it a necessary condition that the new product proposed to be offered by the requesting undertaking competes with other products on a existing market? It is clear that a refusal would not be considered as an infringement if the dominant undertaking refuses to supply others on another market where the dominant undertaking is not present.<sup>153</sup> Compulsory license applies only when the dominant undertaking operates its business on the downstream market.<sup>154</sup> However, an existing downstream market where the dominant undertaking does not engage in any business is different with a potential downstream market that has not yet been established. It is reasonable not to require a dominant undertaking to predict potential compulsory licensing in a market where it is not present.<sup>155</sup> But it would not be logical that a cutting-edge product, which may be capable of creating a new and not yet existing market, would hardly justify a compulsory license.<sup>156</sup> It is therefore argued to be too prescriptive that the new product should compete with the dominant undertaking’s own product.<sup>157</sup> On the one hand, other situations that are capable of causing prejudice to consumers may also be sufficient to invoke Article 102(b);<sup>158</sup> on the other hand, if a new product should be confined to the same market with the dominant undertaking’s product and the new product is required to meet

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<sup>151</sup> Discussion Paper, *supra* note 26, Para 233.

<sup>152</sup> See also Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), pp.124-25.

<sup>153</sup> i.e. Judgment of 12 June 1997, *Ladbroke v Commission*, T-504/93, ECR, ECLI:EU:T:1997:84.

<sup>154</sup> John Temple Lang, ‘The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner’ (2000) 1 *Journal of Network Industries* 375, p385.

<sup>155</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at

<http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p153. See also in John Temple Lang, ‘Anticompetitive Non-Pricing Abuses under European and National Antitrust Law’, in Barry Hawk (ed.) *International Antitrust Law & Policy: Fordham Corporate Law2003* (Juris Publishing, 2004)235, p271.

<sup>156</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p449. See also Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p153.

<sup>157</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p449.

<sup>158</sup> *ibid.*



previously unsatisfied demand by its product differentiation, it would result in market expansion and in turn give rise to re-defining the scope of the relevant market.<sup>159</sup>

Nevertheless, the practical difficulty lies in how to predict what kind of new market the potential new product will create and the scope of that new market.<sup>160</sup> Potential downstream markets, according to the predictability of the potential new product, may fall into two types: *distant future market*<sup>161</sup> and *imminent future market*<sup>162</sup>. *Distant future market* describes the situation where R&D process of a potential new product is at a relatively early stage, and the scope of the potential downstream market is uncertain,<sup>163</sup> while the term *imminent future market* stands for a fairly predictable R&D process with a high likelihood of success, clearer market boundaries and attractiveness to consumers.<sup>164</sup> For the competitors, it might be more convincing if they could demonstrate that in the near future the potential new product would create a new and not yet existing downstream market.

## 4.2 Market dominance

### 4.2.1 IPR, market share and market power<sup>165</sup>

Once the relevant market has been defined and two markets requirement has been satisfied, EU competition authorities will assess whether the IPR holder is in a dominant position on the upstream market, which enables the undertaking concerned to “behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers”.<sup>166</sup> Before

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<sup>159</sup> *ibid.*

<sup>160</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p153.

<sup>161</sup> Marcus Glader, *Innovation Markets and Competition Analysis: EU Competition Law and US Antitrust Law* (Edward Elgar, 2006), pp.237, 303.

<sup>162</sup> *Ibid.*, p248, 306.

<sup>163</sup> *Ibid.*, p237, 303.

<sup>164</sup> *Ibid.*, p248, 306.

<sup>165</sup> Market dominance, or monopoly power in US antitrust law, is a legal concept; while market power illustrates the strength of an undertaking in a defined market from the economic perspective, Moreover, a firm is considered to have market power once it is active on a given market, but market dominance, or monopoly power, exists only when the firm’s market power reaches a certain degree. See Josef Drexel, ‘The Relationship between the Legal Exclusivity and Economic Market Power’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, p15 and fn 3. See also James Kavanagh, Neil Marshall and Gunnar Niels, ‘Reform of Article 82 EC: Can the Law and the Economics be Reconciled?’ in Ariel Ezrachi (ed) *Article 82 EC: Reflections on its Recent Evolution* (Hart Publishing, 2009) 1, p3.

<sup>166</sup> See Judgment in *United Brands* ECLI:EU:C:1978:22, Para 65; Judgment in *Hoffmann-La Roche*, 85/76,

entering into the appraisal of market power, it shall be borne in mind that “what is prohibited is the abuse, not the dominant position or the abuser’s ability to continue in the relevant market and to exploit his various property rights”.<sup>167</sup> The possession of a dominant position should not be condemned, unless the dominant undertaking has failed to assume the special responsibility imposed upon him not to impair undistorted competition on the common market.<sup>168</sup>

It has been declared repeatedly by the EU Courts that mere ownership of IPR does not inevitably confer a dominant position.<sup>169</sup> A similar conclusion has also been reached in US.<sup>170</sup> However, IPR could work as a key for successful market entry, possession of which, especially an essential IPR, may indicate a high possibility of a dominant position.<sup>171</sup> This is more likely when the Commission defines relevant product market narrowly, particularly in cases of single product market where the IPR holder enjoys a *de facto* monopoly. IPR protection normally allows an undertaking to obtain and consolidate its market power by *negatively* keeping other competitors (actual and potential) out of its realm rather than by *positively* promoting the sale of relevant products. Regarding the potential competitive constraints from outside, the role of IPR as a barrier to entry for potential competitors has been noticed owing to an enhanced

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ECLI:EU:C:1979:36, Para 38.

<sup>167</sup> *Hewlett – pachard development company LP, Compaq Trade Mark BV v. Expansys UK Ltd*, 2005 E.T.M.R at 1307 (decision of 14 July 2005)

<sup>168</sup> Judgment in *Nederlandsche Banden Industrie Michelin*, 322/81, ECLI:EU:C:1983:313, Para57.

<sup>169</sup> See e.g. Judgment in *Deutsche Grammophon Gesellschaft mbH v Metro-SB-Grossmarkete GmbH & Co*, 78/70, ECLI:EU:C:1971:59, Para 16-17: “A manufacturer of sound recordings who holds a right related to copyright does not occupy a dominant position within the meaning of Article [102] of the Treaty merely by exercising his exclusive right to distribute the protected articles...this further requires that the manufacturer, alone or jointly with other undertakings in the same group, should have the power to impede the maintenance of effective competition over a considerable part of the relevant market, having regard in particular to the existence of any producers marketing similar products and to their position on the market.” See also Judgment in *Magill* ECLI:EU:C:1995:98, *supra* note 27, Para 46; Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, *supra* note 27, Para 690. Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches But No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008), pp.61-62; Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights: the Regulation of Innovation* (second edition, Oxford University Press, 2011), pp.58-59.

<sup>170</sup> *Illinois Tool Works Inc. et al. v. Independent Ink, Inc.*, 547 U.S. 28 (2006), at 7.

<sup>171</sup> Josef Drexler, ‘The Relationship between the Legal Exclusivity and Economic Market Power’ in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, pp.16-18. See also Herbert Hovenkamp, Mark Janis and Mark Lemley, ‘Chapter 4: Intellectual Property and Market Power’, in *IP and Antitrust: An Analysis of Antitrust Principles Applied to Intellectual Property Law* (Aspen Law & Business, 2002).

understanding of the potential contestability of market.<sup>172</sup> As a possible barrier to entry, IPR would impact the competitive process even more than a relatively high market share.

Market share may as an indicator illustrate what the role the undertaking concerned plays in a relevant market. Given that relevant markets have been defined narrowly in IPR cases, the market share of the accused undertaking usually is relatively high. A high market share by itself, however, does not suffice to establish dominance, especially in the dynamically competitive industries. The EU Commission has construed market share as a “useful indication” rather than a conclusive factor.<sup>173</sup> The Commission would also take into account of the market shares of other competing undertakings in the relevant market, dynamics of the market, product differentiation, barriers to expansion and entry, and countervailing buying power.<sup>174</sup> Other factors like legal regulation, vertical integration, economies of scale, access to financial resources and need for investment, advertising, reputation, opportunity costs and unavoidable trading partner shall also be taken into consideration.<sup>175</sup> The consumers may be locked due to other competitive advantages such as first mover advantage, better distribution system, network effect and good reputation. On the other hand, low market share is not always equal to non-dominance. In the Commission Guidance, it maintains that:

“[D]ominance is not likely if the undertaking’s market share is below 40% in the relevant market. However, there may be specific cases below this threshold where competitors are not in a position to constrain effectively the conduct of a dominant undertaking, for example where they face serious capacity limitations. Such cases may also deserve attention on the part of the Commission.”<sup>176</sup>

It appears the undertaking with a market share under 40 percent is likely to stay in a safe harbour. This harbour is nonetheless not completely safe as it is at the discretion of the EU Commission to determine whether to initiate an investigation. On the one hand it would be legally uncertain for the undertakings with lower market share; on the other hand, the Commission would be imposed on a higher burden to prove the existence of significant market power even in the absence of the possession of an obviously high market share. However, compared to the lower 25 percent threshold provided in the Discussion Paper, it reserves the

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<sup>172</sup> See e.g. Andreas Heinemann, ‘The Contestability of IP-Protected Markets’, in Josef Drexler (ed.), *Research Handbook on Intellectual Property and Competition Law* (Edward Elgar, 2008) 54.

<sup>173</sup> Commission Guidance, *supra* note 26, Para 13.

<sup>174</sup> *ibid*, Para 13-18.

<sup>175</sup> *ibid*, Para 17. See also Discussion Paper, *supra* note 26, Para 40.

<sup>176</sup> Commission Guidance, *supra* note 26, Para 14.

Commission's scarce resources on the more harmful exclusionary practices.<sup>177</sup>

#### 4.2.2 Dominance in 'dynamically competitive industries'

The involvement of IPR and participation of merely one or a few undertakings with high market share in the relevant market are two elements that typically appear in these so-called 'dynamically competitive industries' (or named as 'new economic industries'). These industries include computer software/hardware, internet, telecommunication, biotechnology, pharmaceuticals and other newly developed industries.<sup>178</sup> Though generally these industries are not immune from competition intervention,<sup>179</sup> the possession of intellectual property and/or a high market share in these industries, as elaborated hereinafter, may not be as convincing as in other industries to indicate a dominance power.

These industries contain several common characteristics, as Posner observes, "falling average costs (on a product, not firm, basis) over a broad range of output, modest capital requirements relative to what is available for new enterprises from the modern capital market, very high rates of innovation, quick and frequent entry and exit, and economies of scale in consumption".<sup>180</sup> Two main features could be identified in order to make a proper market power analysis: economies of scale and dynamical competition for the market. While the former gives rise to a rational expectation that the IPR holder would possess significant market power for a certain period,<sup>181</sup> the latter on the other hand indicates that the successful innovator is always under competitive constraint.<sup>182</sup>

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<sup>177</sup> See Discussion Paper, *supra* note 26, Para 31.

<sup>178</sup> David S. Evans and Richard Schmalensee, 'Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries' (2002) 2 *Innovation Policy and the Economy* 1, p5.

<sup>179</sup> Speech of Director-General for Competition Alexander Italianer, 'Prepared remarks on: Level-playing field and innovation in technology markets', at Conference on Antitrust in Technology, Palo Alto (US), 28 Jan 2013, available at [http://ec.europa.eu/competition/speeches/text/sp2013\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2013_01_en.pdf), last visited on 20 July 2014, p3. Cecilio Madero Villarejo, 'Abuses of a Dominant Position in Information Technology Industries (IT)', in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?*, p523.

<sup>180</sup> Richard A. Posner, 'Antitrust in the New Economy', *John M. Olin Law & Economics Working Paper* No. 106 (second series), 2000, p1. See also Richard J. Gilbert and Willard K. Tom, 'Is Innovation King at the Antitrust Agencies? The Intellectual Guidelines Five Years Later', (2001) 69 *Antitrust Law Journal* 43, p45.

<sup>181</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, 'DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries', available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p13.

<sup>182</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, 'DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries', available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p16; David S.

(1) Economic features: economies of scale

Dynamically competitive industries demonstrate significant economies of scale both from the supply side and the demand side. The supply-side economies of scale, or in other words “increasing returns”, is easily noticed in the sense that compared to the old economy industries the marginal cost of an additional product is considerably low, even approaching to zero, once the initial investment has been made and the innovation is successful.<sup>183</sup> Software market could be a typical example. A software company, regardless of its market position, may be required to invest heavily in R&D to generate successful new software; in contrast to the initial investment it costs the company nearly nothing to make another copy of this software. While the price of every extra copy keeps stable, the more copies the software company produces and sells, the sooner it could recover his cost and begin to make a profit.

Network effect, the economies of scale from the demand-side, is another feature of dynamically competitive industries. This economies of scale exists in some physical networks, such as telephony and fax machines, and also in some virtual networks like software market and internet-based businesses. The network effect enables a product to raise its value with the increasing amount of its buyers.<sup>184</sup> The common standards and interoperability in these networks play a critical role to connect its users.<sup>185</sup> The more people make use of it, the more

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Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, p10; Cecilio Madero Villarejo, ‘Abuses of a Dominant Position in Information Technology Industries (IT)’, in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?*, p525.

<sup>183</sup> David S. Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, p8. See also William M. Landes and Richard A. Posner, ‘An Economic Analysis of Copyright Law’ (1989) 18(2) *Journal of Legal Studies* 325, p326. Though some old-economy industries such as gas or electricity are subject to supply-side economies of scale, marginal costs in these industries could not be close to zero.

<sup>184</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p14. David S. Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, p9. Kathryn McMahon, ‘Interoperability: “Indispensability” and “Special Responsibility” in High Technology Markets’, (2007) 9 *Tulane Journal of Technology & Intellectual Property*, 123, p131. Cecilio Madero Villarejo, ‘Abuses of a Dominant Position in Information Technology Industries (IT)’, in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?*, p524.

<sup>185</sup> Speech of Director-General for Competition Alexander Italianer, ‘Prepared remarks on: Level-playing field and innovation in technology markets’, at Conference on Antitrust in Technology, Palo Alto (US), 28 Jan 2013, available

attractive it will be for the people outside of this network. It allows the successful innovator to prevent from being taken over by his competitors either as a barrier to entry, or by leading to “the tipping of the market”;<sup>186</sup> on the other hand it is also an attraction encouraging the competitors to capture the leadership in the market. A business-to-business (B2B) internet business has a two-way network effect. The more buyers use a B2B site, the more sellers would be willing to put their products on that marketing channel, and *vice versa*.<sup>187</sup> This stronger network effect, referred as ‘positive feedback loop’ in IT industry, also exists in the operating platform software and the applications developed for the specific platform.<sup>188</sup> Microsoft’s Windows operating system, with numerous applications compatible with that platform, has demonstrated the attractiveness of that operating system and also its lock-in ability.<sup>189</sup> Smartphone platform software could be another example. As illustrated in the graph below, Android and Apple iOS have displayed strong network effects compared to the platforms of Symbian, Blackberry and Windows phone. For the handset consumers, a mobile phone with the platform Android or iOS is more attractive since more applications are available on these platforms; for the application developers, they are more willing to write applications for a platform like Android or iOS with a large user base, which in turn would continue to enlarge the user network.

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at [http://ec.europa.eu/competition/speeches/text/sp2013\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2013_01_en.pdf), last visited on 20 July 2014, p2.

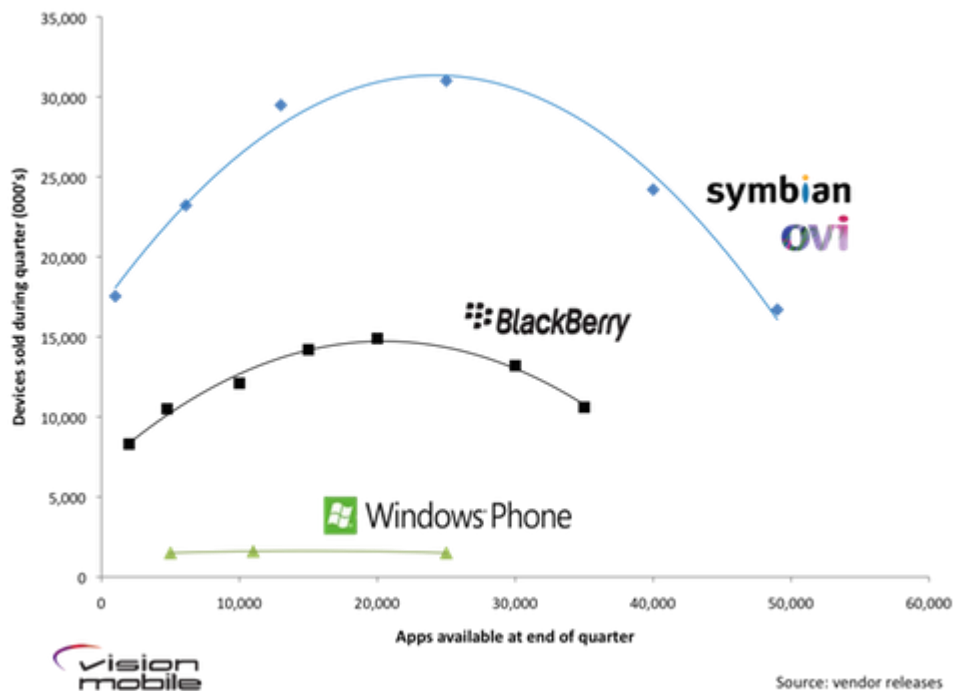
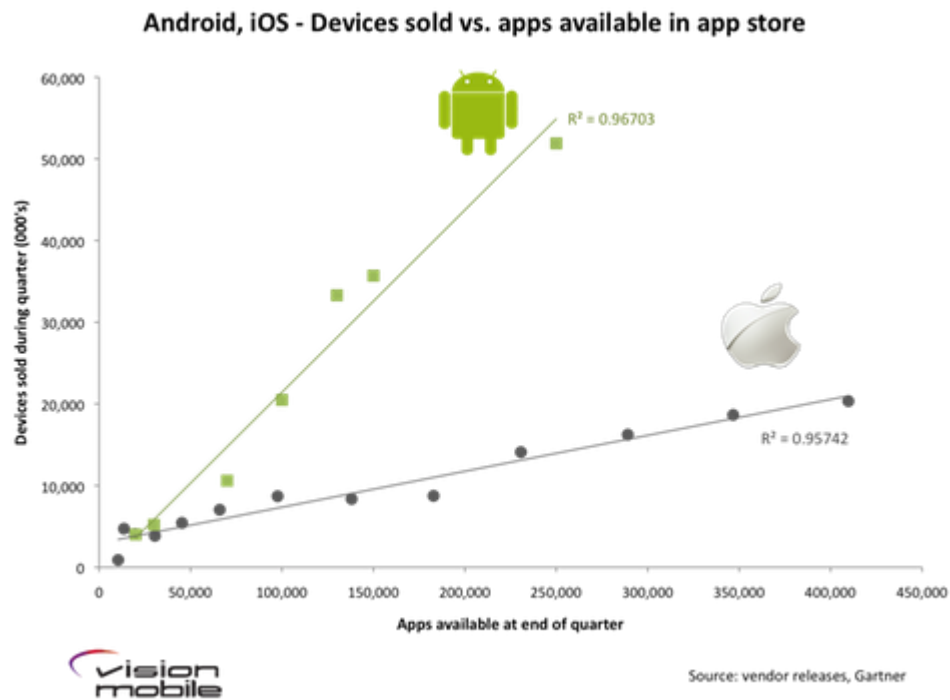
<sup>186</sup> Ibid, p3.

<sup>187</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p14.

<sup>188</sup> Cecilio Madero Villarejo, ‘Abuses of a Dominant Position in Information Technology Industries (IT)’, in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?*, p524.

<sup>189</sup> Case COMP/C-3/37.792 *Microsoft I*, Commission Decision of 24 March 2004, Para 448-464; Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 619. See also Arianna Andreangeli, ‘Interoperability as an “essential facility” in the Microsoft case – encouraging competition or stifling innovation’, (2009) 34 *European Law Review* 587, p593.

Graph 1: network effect in smartphone handset and operating platform markets<sup>190</sup>



<sup>190</sup> The graph is from an online article of an analyst firm VisionMobile, available at <http://www.visionmobile.com/blog/2011/09/the-flywheel-effect-of-android-and-ios-and-why-their-rivals-are-grinding-to-a-halt/>, last visited on 2 Feb 2013.

After all, network effect should not be exaggerated because switching to other networks or systems is not impossible for the users. For instance, in Facebook/WhatsApp merger case<sup>191</sup>, the EU Commission held that, although there are 1.3 billion Facebook platform users worldwide, the network effects could be mitigated by a number of factors – such as the fact that the consumer communications applications market is a fast growing market with short innovation cycles and that consumers can easily switch from one application to another.<sup>192</sup> The possibility of taking over the dominant position by a superior product would constantly incentivize the competitors to challenge the current market winner.<sup>193</sup>

## (2) Economic features: dynamical competition for the market

On the one hand, competition in these industries is a game of “winner-takes-most”, which typically results in a successful market leader with a large market share.<sup>194</sup> Such a market leadership, together with other factors such as economies of scale from supply side, network effect, high switching cost, first mover advantage, superior technology based on previous heavy investment, allow the incumbent to lock in many consumers and enjoy substantial profits.

On the other hand, the achievement in the current race of competition does not guarantee that the market leadership could still be held after another race or several races of competition.<sup>195</sup> The belief that the degree of competition is determined largely by market structure has been proved to be not appropriate.<sup>196</sup> A period of stability in market position does not indicate that the competition is weak, or that the market structure in the near future will not be changed. On the contrary, even these industries have gravitated towards concentrated market structures, leapfrogging innovations have emerged constantly in the history of these new economy

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<sup>191</sup> Case M.7217, EU Commission’s decision of 3 October 2014 approving acquisition of WhatsApp by Facebook, the decision is not yet published.

<sup>192</sup> See Commission’s press release on Facebook/WhatsApp acquisition case, available at [http://europa.eu/rapid/press-release\\_IP-14-1088\\_en.htm](http://europa.eu/rapid/press-release_IP-14-1088_en.htm), last visited on 10 October 2014.

<sup>193</sup> Kelvin Hiu Fai Kwok, ‘A New Approach to Resolving Refusal to License Intellectual Property Rights Disputes’, (2011) 34(2) *World Competition* 261, p277. See also in Kathryn McMahon, ‘Interoperability: “Indispensability” and “Special Responsibility” in High Technology Markets’, (2007) 9 *Tulane Journal of Technology & Intellectual Property* 123; Alan Devlin, ‘Analyzing Monopoly Power Ex Ante’, (2009) 5 *NYU Journal of Law and Business* 153.

<sup>194</sup> Christian Ahlborn, David S. Evans and A. Jorge Padilla, ‘Competition Policy in the New Economy: Is European Competition Law up to The Challenge?’ (2001) 22(5) *European Competition Law Review* 156, p162.

<sup>195</sup> David S. Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, p12.

<sup>196</sup> Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p916.



industries.<sup>197</sup> The *Moore's law* (by Intel's co-founder Gordon Moore) in ICT industry, which follows an 18-month cycle, has been alleged to be shortened to a 6-month cycle due to the rapid development of the mobile internet business.<sup>198</sup> The rapid development of the market for the mobile operating systems has witnessed the fall of the Nokia's Symbian platform system and the rise of apple's iOS and the Android platform. While the former's global market share plummeted from its peak of 52% by 2008 to merely 2.6% by the third quarter of 2012, the market share of Android rocketed up from 3.9% in 2009 to 72.4% and iOS from its first entry in 2007 to 13.9% by the third quarter of 2012.<sup>199</sup> The rising of smartphone's market share in US, as illustrated in Graph 2 below, could also be an example to demonstrate the drastic change of market structure in the dynamically competitive industries. The data shows that smartphone manufacturers took from feature phone producers nearly 21 percent subscribers in US mobile phone market in less than 2 years, and new users of smartphones arrived at an equal amount of feature phones subscribers in spring 2012. The successful smartphone penetration has also been reported in other countries, particularly in developed countries.<sup>200</sup>

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<sup>197</sup> i.e. in the market for word processors software, former leading software WordPerfect (50% market share in 1990) was replaced by Microsoft Word (90% market share in 1997); the dominant position of the market for spreadsheets software was transferred to Microsoft Excel (90% market share in 1997) from Lotus 1-2-3 (70% market share in 1988). See David S. Evans and Richard Schmalensee, 'Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries' (2002) 2 *Innovation Policy and the Economy* 1, p11. There is an opposite view arguing that in these industries there is a need to foster competition in the market because competition for the market takes place slower than expected. See speech of Director-General for Competition Alexander Italianer, 'Prepared remarks on: Level-playing field and innovation in technology markets', at Conference on Antitrust in Technology, Palo Alto (US), 28 Jan 2013, available at [http://ec.europa.eu/competition/speeches/text/sp2013\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2013_01_en.pdf), last visited on 20 July 2014, p4.

<sup>198</sup> China Academy of Telecommunication Research of Ministry of Industry and Information Technology's *Mobile Internet White Paper (2013)*, available at <http://www.catr.cn/kxyj/qwfb/bps/201303/P020130301397809834073.pdf>, last visited on 5 March 2013, p2.

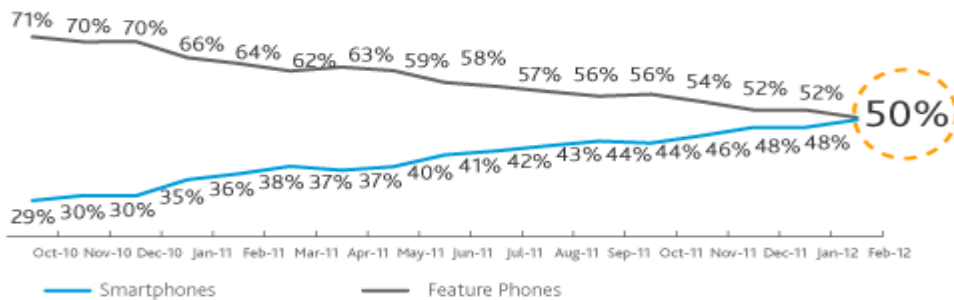
<sup>199</sup> *ibid*, p4.

<sup>200</sup> The analyst firm comScore's research shows that smartphone penetration of EU5 (UK, DE, FR, ES and IT) reached 54.6 percent in October 2012, respectively 63.2% in Spain, 62.3% in UK, 51.4% in France, 51.2% in Italy and 48.4% in Germany. Available at [http://www.comscore.com/Insights/Press\\_Releases/2012/12/EU5\\_Smartphone\\_Penetration\\_Reaches\\_55\\_Percent\\_in\\_October\\_2012](http://www.comscore.com/Insights/Press_Releases/2012/12/EU5_Smartphone_Penetration_Reaches_55_Percent_in_October_2012), last visited on 3 Feb 2013; comScore's research on the smartphone market in Japan shows that smartphone penetration in Japan arrived at 23.5% in summer 2012, growing 43% from the end of 2011. Available at [http://www.comscore.com/Insights/Press\\_Releases/2012/8/Japan\\_Smartphone\\_Surge](http://www.comscore.com/Insights/Press_Releases/2012/8/Japan_Smartphone_Surge), last visited on 3 Feb 2013.

Graph 2: market share of smartphone and feature phone in the US<sup>201</sup>

### U.S. Smartphone Penetration

February 2012, Nielsen Mobile Insights



Read as: During February 2012, 50 percent of US mobile subscribers owned a smartphone

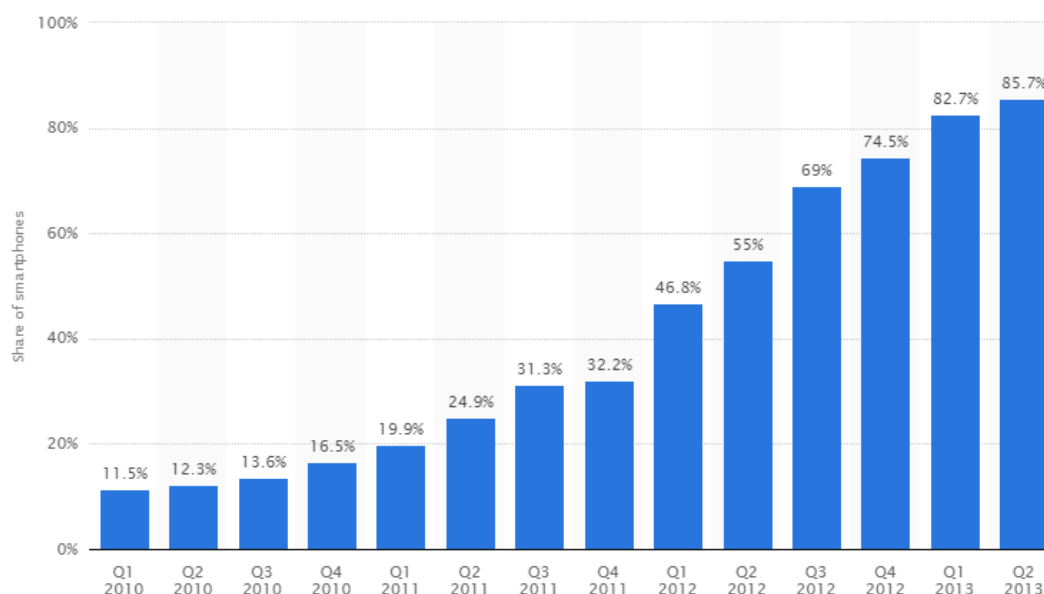
Source: Nielsen

nielsen

The graph 3 below illustrates that some of these dynamically competitive industries, such as the smartphone market, grow even faster particularly in China.

<sup>201</sup> The graph is from an online article of the market analyst firm Nielsen, available at [http://blog.nielsen.com/nielsenwire/online\\_mobile/smartphones-account-for-half-of-all-mobile-phones-dominate-new-phone-purchases-in-the-us/](http://blog.nielsen.com/nielsenwire/online_mobile/smartphones-account-for-half-of-all-mobile-phones-dominate-new-phone-purchases-in-the-us/), last visited on 2 Feb 2013. The comScore's report in June 2014 has demonstrated that the market share of smartphone in the US during the three months ending in April 2014 increased to 69.6 percent, see <http://www.comscore.com/Insights/Press-Releases/2014/6/comScore-Reports-April-2014-US-Smartphone-Subscriber-Market-Share>, last visited on 8 October 2014.

Graph 3: share of smartphones in total cell phone sales in China from the 1<sup>st</sup> quarter of 2010 to the 2<sup>nd</sup> quarter of 2013 (source: statista)<sup>202</sup>



By developing new innovations to destroy old market structure and take over the dominant position, the competitors engage in the competition *for the market*, rather than competition *in the market* through traditional price or output competition in the old economy industries.<sup>203</sup> The process of competition *for the market* is also known as “creative destruction”.<sup>204</sup> Accordingly, the leading companies are under permanent competitive constraints, particularly from the potential innovating competitors.<sup>205</sup> Thus, the incumbent would feel in a competitive

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See

<http://www.statista.com/statistics/238450/share-of-smartphones-in-the-total-sales-volume-of-cell-phones-in-china/>, last visited on 8 October 2014.

<sup>203</sup> David S. Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, pp.1-2. The drastic competition in these industries could be proved by the facts that only five firms from the 1970 and 1985 lists of the US top 20 largest firms ranked by market value were still in the list of top 20 of the year 2000, and more than the half of the firms on the list of the year 2000 were not created in 1970 such as Microsoft and Cisco Systems. See the same article in pp.3-4.

<sup>204</sup> Joseph A. Schumpeter, *Capitalism, Socialism and Democracy* (Taylor & Francis e-Library edition, George Allen & Unwin, 2003), chapter VII, pp.81-85.

<sup>205</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p26. David S. Evans and Richard Schmalensee, ‘Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries’ (2002) 2 *Innovation Policy and the Economy* 1, pp.18-20; Christian Ahlborn, David S. Evans and A. Jorge Padilla, ‘Competition Policy in the New Economy: Is European Competition Law up to The Challenge?’ (2001)

situation, even he is in such a position that the government competition law specialists may currently not even see any effective competition on the relevant market.<sup>206</sup> Additionally, competitive constraints from outside may also impact the pricing policy of the dominant undertaking. The higher the current prices are, the more willing potential competitors will be to entry into this market and the more attractive their products will be to the consumers.<sup>207</sup>

As long as network effects in these industries have not advanced to a *de facto* standard, fierce competition *for the market* may not be excluded.<sup>208</sup> Therefore, traditional techniques employed in old economy industries may not be reliable. A crucial element of a proper market power inquiry is that supply-side constraints, or in other words potential innovative threats should be included in the consideration.<sup>209</sup> Thus the market power examination in a dynamically competitive industry case involves not only the boundary of the relevant market and the market structure as in old economy industries, but also the nature and pace of future competition races for the dominance, the ownership and development of relevant un-commercialized intellectual property rights, the control of other critical facilities, the new products R&D pattern.<sup>210</sup>

## 5. Modernized measures to deal with infringements

### 5.1 Administrative decisions

#### 5.1.1 Interim measure

An entirely new type of administrative decisions has been available since the effective of Council Regulation 1/2003,<sup>211</sup> which enables the Commission to adopt an interim measure

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22(5) *European Competition Law Review* 156, p162.

<sup>206</sup> Joseph A. Schumpeter, *Capitalism, Socialism and Democracy* (Taylor & Francis e-Library edition, George Allen & Unwin, 2003), p85.

<sup>207</sup> David S. Evans and Richard Schmalensee, 'Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries' (2002) 2 *Innovation Policy and the Economy* 1, p17.

<sup>208</sup> Josef Drexler, 'The Relationship between the Legal Exclusivity and Economic Market Power' in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, pp.21-22.

<sup>209</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, 'DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries', available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p22; David S. Evans and Richard Schmalensee, 'Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries' (2002) 2 *Innovation Policy and the Economy* 1, p18.

<sup>210</sup> David S. Evans and Richard Schmalensee, 'Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries' (2002) 2 *Innovation Policy and the Economy* 1, pp.18, 20 and 34.

<sup>211</sup> Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid

when a case is still ongoing. The Commission, acting on its own initiative, may adopt such decision only if the following requirements are met: (1) it is “urgent due to the risk of serious and irreparable damage to competition”; (2) there is “a *prima facie* finding of infringement”.<sup>212</sup> The same article provides that “[i]nterim measures must be for a limited period of time and may be renewed in so far as is necessary and appropriate”.<sup>213</sup> The form of the remedies in an interim decision is in general the same as that would be adopted in an infringement decision. Normally behavioural remedies would be applied. In *IMS Health*, the Commission requested the holder of 1860 brick structure to negotiate a copyright license with its competitor in the interim decision.<sup>214</sup> It might not be effortless to interpret the condition which requires the appearance of urgency due to the risk of serious and irreparable damage to competition. While the evaluation of a *serious* harm depends on a case-by case basis analysis, it is clearly ruled by the General Court in *La Cinq*<sup>215</sup> that to assess whether there is an *irreparable* damage, what the Commission need to consider is whether the damage will “no longer be remedied by the decision to be adopted by the Commission upon the conclusion of the administrative procedure”, but not beyond what is necessary to assess whether the damage “cannot be remedied by any subsequent decision” which includes the decision of EU Courts or Member States’ courts.<sup>216</sup> For the question whether there is a clear causal relationship between *urgency* and *serious and irreparable damage*, or in other words whether or not *urgency* and *serious and irreparable damage* are cumulative requirements, the General Court has given its answer in *IMS Health* that “if a risk of serious and irreparable harm exists, urgency is inevitably simultaneously established”.<sup>217</sup> *IMS Health* is also a case where the Commission and the Court had dispute on interpreting *serious and irreparable damage* in practice. The interim decision issued by the Commission was based on the finding that there was a high risk that the competitors would be eliminated from the market.<sup>218</sup> However, the president of the General Court on the contrary concluded that the risk was not as high as estimated by the Commission and thus suspended the decision. It is worth noting that the order from the president of the General Court put forward a balancing approach, which put both the possible harm to the incumbent and the harm to the competitors on the scale. The grant of an interim measure,

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down in Article 81 and 82 of the Treaty (hereinafter ‘Regulation 1/2003’), [2003] OJ L1/1.

<sup>212</sup> *ibid*, Art. 8(1).

<sup>213</sup> *ibid*, Art. 8(2).

<sup>214</sup> COMP D3/38.044 *IMS Health*, *supra* note 66, Art. 2.

<sup>215</sup> Judgment of 24 January 1992 *La Cinq SA v. Commission*, T-44/90, ECR, ECLI:EU:T:1992:5.

<sup>216</sup> *Ibid*, Para 79-80.

<sup>217</sup> Judgment of 26 October 2001, *IMS Health v Commission*, T-184/01 R, ECR, ECLI:EU:T:2001:259, Order of the President of the General Court, *supra* note 67, Para 54.

<sup>218</sup> COMP D3/38.044 *IMS Health*, *supra* note 66, Para 190-201.

according to the order, should only be possible under the circumstance that the irreparable detriment to the effective competition in the absence of such interim measure, namely the elimination of all other competitors in the market, clearly outweighs the potential damage to the dominant undertaking when such an interim decision is granted.<sup>219</sup> There might be two reasons to explain why refusal to license cases may not be the appropriate cases to adopt interim measures. Firstly, interim decision is an administrative measure which by its nature is inclined to protect the short term interests of the specific victim or the competitive conditions from being irreparably damaged, while in refusal to license cases the long term interests – such as the incentive of the accused undertaking and other undertakings to innovate and to invest, the long term consumer welfare – shall also be taken into consideration. Secondly, the balancing test put forward by the president of the General Court in *IMS Health* requires the Commission to decide whether the possible harm to the incumbent outweigh the harm to the competitors when imposing an interim measure, which normally is a compulsory license order in a refusal to license case, while in practice such a comparison would be difficult, or even impossible to make until the end of the whole assessment that however leads to the final decision of the Commission. In the foregoing analysis, theoretically and practically, interim measure might not be the proper choice for the Commission in the refusal to license cases where the competition authority would normally be at pains for several years like in *Microsoft* case to conduct the assessment and make a decision based on all relevant circumstances.

### 5.1.2 Commitment decision

Commitment decision is another new instrument laid down in Regulation 1/2003.<sup>220</sup> Accused undertakings could, on their own initiative, propose commitments to meet the Commission's concern during the investigation. The Commission is not obliged to approve such commitments and bring the investigations to an end. This often takes place when the commitments offered are regarded to be not effective enough to address the Commission's concerns.<sup>221</sup> If such specific commitments are adopted, the Commission would publish a binding commitment decision on the undertaking concerned.<sup>222</sup> There is no longer grounds for the Commission to determine whether the accused conduct has infringed competition rules unless the proceeding, upon request or on the Commission's own initiative, is re-opened when any of following situations occurs: "(1) where there has been a material change of the facts on which the decision was

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<sup>219</sup> Judgment of 26 October 2001, *IMS Health v Commission*, T-184/01 R, ECR, ECLI:EU:T:2001:259, Order of the President of the General Court, *supra* note 67, Para 125-129.

<sup>220</sup> Regulation 1/2003, *supra* note 211, Art. 9.

<sup>221</sup> But the Commission is not required to explain why the commitments offered are not appropriate to address its concern. See e.g. Judgment of 11 July 2007, *Alsora v Commission*, T-170/06, ECR, ECLI:EU:T:2007:220, Para 130.

<sup>222</sup> Regulation 1/2003, *supra* note 211, Art. 9(1).

based; (2) where the undertakings concerned has infringed their commitments; or (3) where the decision was based on incomplete, incorrect or misleading information provided by the parties”.<sup>223</sup>

Since 2004 more and more undertakings, mainly in the information and communication technology sector and energy sector, have offered binding commitments to efficiently address the anti-competitive concern.<sup>224</sup> The accused undertakings are more willing to provide commitments, on their own initiative, on the grounds that, apart from escaping them from a potentially time-consuming and exhausting investigating process, commitment decisions have reputational advantage (no infringement would be established) and financial advantage (no fine will be imposed in a commitment decision, and that decision could not be used as an infringement finding for private competition lawsuits requiring imposition of a fine in Member States) for the undertakings.<sup>225</sup> The EU Commission welcomes this cooperative attitude of the undertakings and also makes efforts to bring the cases to an end with more timely, effective and lasting solutions.<sup>226</sup> The more rapidly the anti-competitive practices are terminated in

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<sup>223</sup> *ibid*, Art. 9(2). To date the *Microsoft* browser choice case is the first case where the Commission found a breach of legally binding Art. 9 commitment decision (Case COMP/C-3/39.530, commitment decision was issued on 16 December 2009. EU Commission opened proceedings against Microsoft to investigate possible non-compliance with its commitments on 17 July 2012 and imposed a 561 million euro fine on Microsoft on 6 March 2013, see press release at [http://europa.eu/rapid/press-release\\_IP-13-196\\_en.htm](http://europa.eu/rapid/press-release_IP-13-196_en.htm), last visited on 20 July 2014).

<sup>224</sup> Article 102 cases ended with binding commitment decisions include, for instance, Coca-Cola (Case COMP/A.39.116/B2, commitments decision on 22 June 2005); De Beers (Case COMP/B-2/38.381, commitments decision on 22 February 2006); Distrigaz (Case COMP/B-1/37.966, commitments decision on 11 October 2007); E.ON German electricity market (Cases COMP/39.388 and COMP/39.389, commitments decision on 26 November 2008); RWE gas foreclosure (Case COMP/B-1/39.402, commitments decision on 18 March 2009); Gaz de France (Case COMP/B-1/39.316, commitments decision on 3 December 2009); Rambus (Case COMP/C-3/38.636, commitments decision on 9 December 2009); Microsoft browser choice (Case COMP/C-3/39.530, commitments decision on 16 December 2009); EDF long term electricity contracts in France (Case COMP/39.386, commitments decision on 17 March 2010, modified on 11 August 2010); Swedish Interconnectors (Case COMP/39.351, commitments decision on 14 April 2010); E.ON Gas (Case COMP/B-1/39.317, commitments decision on 4 May 2010); ENI (Case COMP/B-1/39.315, commitments decision on 29 September 2010); Standard & Poor's (Case COMP/39.592, commitments decision on 15 November 2011); IBM maintenance services (Case COMP/C-3/39.692, commitments decision on 13 December 2011); CEZ (Case COMP/39.727, commitments decision on 10 April 2013).

<sup>225</sup> See e.g. Heike Schweitzer, 'Commitment Decisions under Art.9 of Regulation 1/2003: the Developing EC Practice and Case Law' (2008) EUI Working Papers Law No. 2008/22, available at <http://ssrn.com/abstract=1306245>, last visited on 15 Feb 2013, pp1-2; Christopher Cook, 'Commitment Decisions: The Law and Practice under Article 9', (2006) 29(2) *World Competition* 209, pp.210-212.

<sup>226</sup> Speech of Commissioner Joaquín Almunia, 'Recent developments and future priorities in EU competition policy' at *International Competition Law Forum*, St. Gallen, 8 April 2011, SPEECH/11/243, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/11/243&format=HTML&aged=0&language=E>

compliance with competition rules, the less harm they would inflict on the competition process and the consumer, and the more public resources would be saved for the investigations on other behaviours with more anti-competitive effects.<sup>227</sup> However, as a solution consented by both the Commission and the undertakings concerned, the deficiency of the commitment decision lies in that no precedent would be established due to its *settlement* nature.<sup>228</sup> Thus it is argued that commitment decision, as an increasingly popular instrument to escape both the Commission and the undertakings in complex cases from time-consuming procedures, contributes limited experience for the assessment and techniques employed in infringement decisions, which would finally constitute case law under Article 102 TFEU.<sup>229</sup> In this regard, it raises the concern that the broad discretion at the Commission's hand may induce the authority to impose a weakened role on the link between the preliminarily found infringement and the remedy, resulting in the expanding power of the Commission outside of the control of judicial control particularly in the regulating markets.<sup>230</sup> The Court of Justice's hands-off approach on the judicial review of commitment decisions in *Alrosa*<sup>231</sup> would substantially increase that discretion.<sup>232</sup>

Being bilaterally consented, in general the content of a commitment decision would not been

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[N&guiLanguage=en](#), last visited on 1 Oct 2011, “[o]ne trend that is emerging from a growing number of antitrust cases is our search for effective – and sometimes structural – commitments when they would more efficiently prevent competition concerns in the longer term.”

<sup>227</sup> See Heike Schweitzer, ‘Commitment Decisions under Art.9 of Regulation 1/2003: the Developing EC Practice and Case Law’ (2008) EUI Working Papers Law No. 2008/22, available at <http://ssrn.com/abstract=1306245>, last visited on 15 Feb 2013, pp1-2. See also in EU Commission, MEMO/04/217, [http://europa.eu/rapid/press-release\\_MEMO-04-217\\_en.htm](http://europa.eu/rapid/press-release_MEMO-04-217_en.htm), last visited on 22 Feb 2013.

<sup>228</sup> Regulation 1/2003, *supra* note 211, preamble 13. For an overview of benefits and loss of the commitment procedure compared to the infringement procedure, see e.g. Florian Wagner-Von Papp, ‘Best and Even Better Practices in Commitment Procedures after *Alrosa*: The Dangers of Abandoning the “Struggle for Competition Law”’, (2012) 49 *World Competition* 929, pp.956-960.

<sup>229</sup> See Maurits Dolmans, Thomas Graf and David R. Little, ‘Microsoft’s browser-choice commitments and public interoperability undertaking’, (2010) 31(7) *European Competition Law Review* 268, p275.

<sup>230</sup> See Heike Schweitzer, ‘Commitment Decisions under Art.9 of Regulation 1/2003: the Developing EC Practice and Case Law’ (2008) EUI Working Papers Law No. 2008/22, available at <http://ssrn.com/abstract=1306245>, last visited on 15 Feb 2013, pp10-11. See also in EU Commission, MEMO/04/217, [http://europa.eu/rapid/press-release\\_MEMO-04-217\\_en.htm](http://europa.eu/rapid/press-release_MEMO-04-217_en.htm), last visited on 22 Feb 2013; George Stephanov Georgiev, ‘Contagious Efficiency: The Growing Reliance on US-Style Antitrust Settlement in EU Law’, (2007) 2007(4) *Utah Law Review* 971, pp.1031-1032.

<sup>231</sup> Judgment in *Alrosa*, C-441/07 P, ECLI:EU:C:2009:555.

<sup>232</sup> See Florian Wagner-Von Papp, ‘Best and Even Better Practices in Commitment Procedures after *Alrosa*: The Dangers of Abandoning the “Struggle for Competition Law”’, (2012) 49 *World Competition* 929, pp.930-931.



challenged from the part of the undertakings on whom the binding decision has imposed. Therefore, it is crucial to ensure that the commitment decision not only is capable of addressing the competition concern and completely bringing the infringement to an end, but also shall not unduly adjust the infringement to the detriment of the legitimate interests of the undertaking. In other words, the *right* commitment decisions should be issued to the *right* cases. The first concern is to ascertain under what circumstances a commitment decision is appropriate to be adopted. As pointed out in preamble 13 of Regulation 1/2003 and the Commission memorandum on commitment decision, severe infringements of competition law, such as hardcore cartels where a fine might be applicable as punishment, may not be the appropriate cases.<sup>233</sup> It is suggested that proper ‘Article 9 infringements’ shall have restrictive effects that however would not result in irreparable harm, and the anti-competitive effects could be removed by either modifying some aspects of their behaviour or putting an end to some of their conducts.<sup>234</sup> The difficulty in practice is how to identify these cases from those having anti-competitive effects but however could be justified by objective justifications. The conducts in the former cases, without the interruption of commitment decision, would be possibly considered infringement of competition law when the procedure of prohibition decisions continues, while the behaviour in latter cases are not infringements since the pro-competitive elements outweigh the anti-competitive effects. It is difficult to determine in which group a specific case belongs to without an in-depth assessment. However, a comprehensive evaluation, which requires a large amount of time, is the very issue the Commission tends to avoid in commitment decisions. Some dynamically competitive industries, such as the information and communication technology sector, are suggested to be the appropriate sectors to apply commitment procedure.<sup>235</sup> The Commission indeed has been incentivized to choose the commitment procedure mainly because the situations in these industries might be technologically complex and be changing fast, thus the assessment prior to a prohibition decision might require a large amount of data such as technological information, which could be more time-consuming, and thus the decision might be long-delayed.<sup>236</sup> Nevertheless, complexity or newness of the situations in these industries could not justify

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<sup>233</sup> Commission press release MEMO/04/217, 17 September 2004, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/04/217&format=HTML&aged=1&language=EN&guiLanguage=en>, last visited on 15 July 2011.

<sup>234</sup> See Alberto Pera and Michele Carpagano, ‘The Law and Practice of Commitment Decisions: A Comparative Analysis’, (2008) 29(12) *European Competition Law Review* 669, pp.671-762.

<sup>235</sup> See e.g. Christopher J. Cook, ‘Commitment Decisions: The Law and Practice under Article 9’, (2006) 29 *World Competition* 209, p209.

<sup>236</sup> See Florian Wagner-Von Papp, ‘Best and Even Better Practices in Commitment Procedures after *Alrosa*: The Dangers of Abandoning the “Struggle for Competition Law”’, (2012) 49 *World Competition* 929, pp.964.

unduly application of commitment decision by the Commission, since firstly the infringements in these industries, like other traditional industries, have far-reaching impact on the consumer welfare, and secondly these cases may provide great opportunity – such opportunities may be rare – for the Commission to clarify some novel legal issues if it opts for the infringement procedure, which is subject to judicial review.<sup>237</sup>

The second concern is that the content of a commitment decision shall be able to address the Commission's concern without imposing undue restriction for the undertaking concerned. Though the General Court and the Court of Justice disputed on the extent and content of the principle of proportionality, it is no doubt that the principle shall, as a general principle of EU law, be applied in commitment procedure.<sup>238</sup> The decision cannot go beyond what is necessary to eliminate the restrictive effect brought about by the infringement.<sup>239</sup> To be a *right* commitment decision, the Commission may confront with two questions – appropriate choice of binding measure and the duration of that binding measure. Firstly, when there is a choice of

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<sup>237</sup> Ibid, pp.962-963.

<sup>238</sup> Regulation 1/2003, *supra* note 211, preamble 12. The General Court held in Judgment in *Alsora v Commission*, ECLI:EU:T:2007:220: “[A]lthough Article 9 of Regulation No 1/2003 does not, unlike Article 7(1), refer to the principle of proportionality, the Commission is obliged to comply with that principle when it adopts decisions on the basis of Article 9.” (Para 92) The Court of Justice confirmed it in the appeal Judgment in *Alrosa* ECLI:EU:C:2009:555: “[T]he principle of proportionality, as a general principle of European Union law, is none the less a criterion for the lawfulness of any act of the institutions of the Union, including decisions taken by the Commission in its capacity of competition authority.” (Para 36)

However, the courts had different opinions regarding the content and extent of this principle when applied in the commitment procedure. The General Court in *Alrosa* considered the application of this proportionality principle should be almost the same as in the infringement procedure: “[T]he voluntary nature of the commitments also does not relieve the Commission of the need to comply with the principle of proportionality, because it is the Commission's decision which makes those commitments binding. The fact that an undertaking considers, for reasons of its own, that it is appropriate at a particular time to offer certain commitments does not of itself mean that those commitments are necessary.” (Para 105) In the appeal the Court of Justice expressed its divergent view: “Article 9 of that regulation, by contrast, provides merely that in proceedings under that provision, as follows from recital 13 in the preamble to the regulation, the Commission is not required to make a finding of an infringement, its task being confined to examining, and possibly *accepting*, the commitments offered by the undertakings concerned in the light of the problems identified by it in its preliminary assessment and having regard to the aims pursued. Application of the principle of proportionality by the Commission in the context of Article 9 of Regulation No 1/2003 is confined to verifying that the commitments in question address the concerns it expressed to the undertakings concerned and that they have not offered less onerous commitments that also address those concerns adequately. When carrying out that assessment, the Commission must, however, take into consideration the interests of third parties.” (Para 41, 42, emphasis added)

<sup>239</sup> Wouter Wils, ‘Settlements of EU Antitrust Investigations: Commitment Decisions under Article 9 of Regulation No 1/2003’, (2006) 29 *World Competition* 345, pp.351-352.

several remedies, the Commission has to choose the one which is proportionate to meet the concern with less damage to the undertakings concerned.<sup>240</sup> For instance, when behaviour commitment and structure commitment are both capable of eliminating the restrictive effects, behaviour commitment might be the better solution.<sup>241</sup> The second question is the extent to which the proposed commitments limit the undertaking concerned. Normally it relates to the length of the binding commitments imposed on the undertaking concerned. For the competition authority, it could be wrong to base the predication of the future development of the relevant market on the current investigation and thereby issue an excessively long period of binding on the dominant undertakings, whose hands will thus be tied longer than what is necessary.<sup>242</sup> A proportionate length may depend on many relevant aspects including market power of the undertaking concerned, the current market structure, the nature of the market, and the prediction of the development of that market.

## 5.2 Behavioural and structural remedies

Once an abuse of dominance has been found, in order to terminate the infringement and to recover the competitive process in the market, the competition authorities would issue prohibition decisions, in which remedies fall into two categories except for fines: behavioural remedies and structural remedies.<sup>243</sup> Economist F.M. Scherer describes that the difference between behavioural remedies and structural remedies is analogous to the difference in medical treatments between drug therapy and surgery.<sup>244</sup> Behavioural remedies, like drug therapy, are less drastic and consequently take a longer time to cure the patient. Continuous monitoring is required to ensure the behaviour of the dominant undertaking is compliance with its commitments.<sup>245</sup> However, it may be not enough for competition authorities to merely prohibit specific abusive conducts; it should also “pry open to competition a market that has been closed by defendants’ illegal restraints”.<sup>246</sup> Frequently-used behavioural remedies thus may not be always capable of completely bringing the effective competition back to the right track. In

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<sup>240</sup> See Judgment in *Alsora v Commission*, ECLI:EU:T:2007:220, Para 98.

<sup>241</sup> Regulation 1/2003, *supra* note 211, preamble 12.

<sup>242</sup> John Temple Lang, ‘Commitment Decisions and Settlements with Antitrust Authorities and Private Parties under European Antitrust Law’, in Barry E. Hawk (ed.) *2005 Annual Proceedings of the Fordham Corporate Law Institute* 265, p323.

<sup>243</sup> Regulation 1/2003, *supra* note 211, art. 7.

<sup>244</sup> F.M Scherer, ‘A perplexed economist confronts “too big to fail”’, (2010) 7(2) *The European Journal of Comparative Economics* 267, pp.277-278.

<sup>245</sup> *ibid.*

<sup>246</sup> *International Salt Co., Inc. v. United States*, 332 U.S. 392, 401 (1947).

*United Shoe Machinery*<sup>247</sup>, Judge Wyzanski rejected the government's call for a structural remedy and imposed behavioural remedies on the defendant. After a decade, the appellant was back to the court and claimed that the behavioural remedies had failed to recover the competitive conditions in the shoe making equipment market.<sup>248</sup> Finally the case ended with a structural remedy which brought the defendant's market share below thirty-three percent.<sup>249</sup>

Structural remedies, like the surgery, are more effective than behavioural remedies by reducing the market power in a short period but with more pain on the dominant undertaking.<sup>250</sup> This conclusion could also be reached when considering the proper form of the remedy in the commitment procedure.<sup>251</sup> Structural remedies may divide a dominant undertaking into two or more separate companies, as the trial court ordered in *US Microsoft* case – reversed on appeal though<sup>252</sup>, or divest some assets from the dominant undertaking. Although structural remedies could save public resources on subsequent surveillance, it is argued that these measures may be too radical and sometimes on the contrary would lead to loss of scale economies or loss of efficiencies.<sup>253</sup> The potential remedies could be so harsh that an undertaking may feel chilled, hence it may choose a conservative commercial strategy rather than to adopt conducts which are actually pro-competitive and beneficial to consumers. Therefore, the competition authorities are reluctant to adopt them. As the last resort “not to be used indiscriminately”,<sup>254</sup> a structural remedy may only be taken into account when the authorities consider that behavioural remedies are not effective enough to bring the infringement to an end and to get the market back on the competitive track. That may be the reason why structural remedies are often

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<sup>247</sup> *United States v. United Shoe Mach. Corp.*, 110 F. Supp. 295 (D. Mass. 1953), aff'd per curiam, 347 U.S. 521 (1954).

<sup>248</sup> *United States v. United Shoe Mach. Corp.*, 266 F. Supp. 328 (D. Mass. 1967), p330.

<sup>249</sup> *United States v. United Shoe Mach. Corp.*, 391 U.S. 244 (1968). The 33 percent market share approach was put forward by Judge Hand in case *United States v Aluminum Co. of America (Alcoa)* 148 F.2d 416 (1945): “[A] 33 percent market share was insufficient to find monopoly power, 66 percent was possible though doubtful, and 90 percent or more was sufficient”. (p424)

<sup>250</sup> F.M Scherer, ‘A perplexed economist confronts “too big to fail”’, (2010) 7(2) *The European Journal of Comparative Economics* 267, p278.

<sup>251</sup> Speech by Commissioner Joaquin Almunia responsible for Competition Policy, ‘Remedies, commitments and settlements in antitrust’, 08 March 2013, SPEECH/13/210, available at [http://europa.eu/rapid/press-release\\_SPEECH-13-210\\_en.htm?locale=en](http://europa.eu/rapid/press-release_SPEECH-13-210_en.htm?locale=en), last visited on 8 March 2013.

<sup>252</sup> *United States v. Microsoft Corp.*, 97 F. Supp. 2d. 59 (D.D.C. 2000), aff'd in part and rev'd in part, 253 F.3d 34 (D.C. Cir. 2001).

<sup>253</sup> See E. Thomas Sullivan, ‘Antitrust remedies in the US and EU: advancing a standard of proportionality’, (2003) 48 *Antitrust Bulletin* 377, p394; Wei Wang, ‘Structural remedies in EU antitrust and merger control’, (2011) 34(4) *World Competition* 571, pp.588-589.

<sup>254</sup> *Timken Roller Bearing Co. v. U.S.* 341 U.S. 593, 603 (1951).

adopted by the Commission to address competition concern in energy sector, rather than in the dynamically competitive industries where measures like divestures might discourage the incentives to invest and innovation of the incumbent.<sup>255</sup> Referring to ENI case as an example, ENI offered his structural commitment to divest its shareholdings in international gas transmission pipelines (TENP, Transitgas and TAG) to a proper purchaser who is independent and unconnected to ENI.<sup>256</sup> The Commission considered “a behavioural remedy would not only have required relying on additional measures of supervision but moreover would not have been sufficient to fully alleviate the Commission’s concerns”.<sup>257</sup> In other words, without the divesture, there was no effective behavioural remedy that enabled the Commission to remove the incentives of a vertically integrated energy company to again adopt anti-competitive behaviour.<sup>258</sup> Yet, the Commission shall apply this remedy with much caution since a recent Commission study found that only 56% of merger divestiture remedies have “clearly achieved their competition objective”.<sup>259</sup> The same conclusion has been demonstrated under US antitrust law that only AT&T’s break-up in 1984 has been considered to be a success among 23 monopolisation cases ending with structural remedies.<sup>260</sup>

## 6. Preliminary Questions for China

The formulation of competition policy and adoption of specific analytical approaches in the development of a particular country’s competition law closely relate to its situation and development in culture, economy and politics.<sup>261</sup> Therefore, for the developing countries, it is not obliged to follow the largely successful legislation and enforcement models – the EU competition law or the US antitrust law.<sup>262</sup> A particular policy or an analytical approach’s succeed in the EU or the US, does not imply that it could be well applied in other jurisdictions. In determining whether such policy or approach should be transposed, many aspects – such as

<sup>255</sup> Case COMP/39.388, *E.ON German Electricity Wholesale Market* and COMP/39.389, *German Electricity Balancing market* (26 November 2008), OJ 2009/C 36/08; Case COMP/39.402, *RWE Gas Foreclosure* (18 March 2009), OJ 2009/C 133/08; Case COMP/39.315, *ENI*, OJ 2010/C 352/10 (29 September 2010).

<sup>256</sup> Case COMP/39.315, *ENI*, OJ 2010/C 352/10 (29 September 2010), Para 64.

<sup>257</sup> *ibid*, Para 92.

<sup>258</sup> *ibid*, Para 90-91.

<sup>259</sup> See the DG COMP staff paper ‘Merger Remedies Study’ (October 2005), chart 27, available at [http://ec.europa.eu/competition/mergers/legislation/remedies\\_study.pdf](http://ec.europa.eu/competition/mergers/legislation/remedies_study.pdf), last visited on 9 Oct 2011.

<sup>260</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p737.

<sup>261</sup> Maaher M Dabbah, ‘The Development of Sound Competition Law and Policy in China: An (Im)possible Dream’, (2007) 30(2) *World Competition* 341, p354.

<sup>262</sup> *ibid*.

its compatibility with other competition policies and approaches, corresponding requirements on the competition law enforcers, potential responses from the companies and legal consultants – need to be taken into account beforehand.

The Chinese Anti-Monopoly Law<sup>263</sup> has adopted a model similar to the EU scheme of dominance abuse, including for instance the definition of relevant market, the decisive aspects to find a dominance position, classification of specific anti-competitive practices.<sup>264</sup> With respect to refusal to deal, it is explicitly provided that dominant undertakings would be found guilty if they “refuse to trade with a trading partner without any justifiable cause”.<sup>265</sup> But the situation of refusals to trade with a new customer has not been mentioned. It is also unclear how the law will be implemented in refusal to license IPR cases. The AML does not specify whether tangible properties and intellectual properties would be treated in a same manner in refusal cases. With respect to competition issues involving IPR, AML provides that the law “does not govern the conduct of business operators to exercise their intellectual property rights under laws and relevant administrative regulations on intellectual property rights”; the law applies to “business operators’ conduct to eliminate or restrict market competition by abusing their intellectual property rights”.<sup>266</sup> However, what behaviour constitutes *abusing intellectual property rights* has not been clarified.

Article 55 of the AML, like Article 102 TFEU, provides only a basic principle rather than specific rules which could facilitate the legal and economic analysis for competition authorities and relevant courts. Specific guidelines are inevitable complement to a workable analytical framework. While such a guideline is still under discussion in China,<sup>267</sup> the implication from EU model is significant for Chinese competition authorities on the following questions:

(a) While a more effect-based and economic approach has already been introduced in Chinese merger cases, will such an approach be adopted in analyzing the potentially abusive conducts like what has been employed by the EU Commission Guidance?

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<sup>263</sup> Anti-monopoly Law of the People's Republic of China (adopted at the 29th meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China on August 30, 2007). (hereinafter ‘AML’)

<sup>264</sup> Mark Furse, ‘Competition Law Choice in China’, (2007) 30(2) *World Competition* 323, p325; Maaher M Dabbah, ‘The Development of Sound Competition Law and Policy in China: An (Im)possible Dream’, (2007) 30(2) *World Competition* 341, p354. Giacomo Di Federico, ‘The New Anti-monopoly Law in China from a European Perspective’, (2009) 32(2) *World Competition* 249, pp.252, 255-256. See more analysis in chapter 1, section 2.

<sup>265</sup> AML, *supra* note 263, Art. 17(3).

<sup>266</sup> AML, *supra* note 263, Art. 55.

<sup>267</sup> See chapter 5, section 4.2 and 4.3.

(b) As an exception rather than a rule, what conditions will constitute the exceptional circumstances in refusal to license IPR cases in China?

(c) How would ‘justifiable cause’ be interpreted in dominance abuse cases in general, and in refusal to license IPR cases in particular by Chinese competition law enforcers? Will the efficiency defence start to play a role?

## 7. Conclusion

In summary, this chapter investigates some basic issues under Article 102 TFEU framework in order to demonstrate the position held by the EU Commission and the Court of Justice regarding refusal to license IPR. This chapter revisits a series of fundamental EU refusal to license IPR cases, concentrating on the emergence and development of the ‘exceptional circumstances test’ before it has been further modified by the General Court in *Microsoft I* case. Moreover, from the perspective of the EU Commission, the adoption of the Commission Guidance, as the result of Article 102 TFEU modernization after a consultation on the Discussion Paper, has demonstrated a significant shift towards a more economic based approach in relation to abusive exclusionary conducts. Apart from the method to assess the potential abusive conduct, this chapter also analyses two preliminary questions before finding an abuse: defining relevant markets and assessing the existence of dominant position. The two markets requirement should be satisfied for the first question; the second question concerns how to assess the market power in the cases involving intellectual property rights, particularly in the dynamically competitive industries. Additionally, possible measures after finding an infringement (including the administrative measures) and the types of remedies are analyzed in this chapter. The Chinese *Anti-Monopoly Law* has adopted a dominance abuse scheme similar to EU. It will be in-depth elaborated whether and to what extent the current EU criteria on refusal to license could be transposed to the Chinese legal and economic context in chapter 5.





## CHAPTER III The Microsoft case debate – a case study

### 1. The EU Commission's open-ended approach

The EU *Microsoft I* case<sup>1</sup> has attracted a lot of attention within the EU as well as from other jurisdictions. The proceeding of this landmark case took more than 7 years before the 2007 General Court's judgment upheld the 2004 Commission's prohibition decision.<sup>2</sup> Two different abusive conducts of the US software company Microsoft were examined by the Commission: one is refusal to supply interoperability information to its competitors on the market for workgroup server systems, the other concerns Microsoft's bundling its Windows operating system with the software Windows Media Player and selling to customers together. Given the limited scope of this research, only the former behaviour is the subject of this chapter. In brief the facts with respect to the interoperability information issue are as follows<sup>3</sup>: Microsoft held an overwhelmingly dominant position, with its market share of over 90%, on the market for client PC operating systems where network effects are apparently strong.<sup>4</sup> As one of Microsoft's important competitors on the neighbouring market for workgroup server systems, the US company Sun Microsystems complained to the EU Commission alleging that Microsoft had violated Article 102 TFEU by refusing to provide adequate interoperability information which is used to connect client system and server system. In the absence of such information, Sun's workgroup server system was not able to communicate well with Microsoft's server system and its PC operating system. By such refusal Microsoft was capable of leveraging his almost monopoly position on the market for PC operating systems onto the market for workgroup server systems. As a result the competitors on the latter market were not able to compete with Microsoft on a level playing field. Hence the effective competition process was distorted, and the consumers were locked in the Microsoft's products which relied on its privileged

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<sup>1</sup> Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289 (hereinafter this Microsoft interoperability information case will be referred to as '*Microsoft I*', while the Microsoft compliance case, which deals with follow-on pricing issue, will be referred to as '*Microsoft II*' in chapter 4).

<sup>2</sup> The EU Commission opened proceedings against Microsoft on 3 August 2000 and issued a prohibition decision on 24 March 2004, which was upheld by the General Court on 17 September 2007. On 27 June 2012, the General Court upheld a 2008 Commission decision imposing a penalty payment on Microsoft for not complying with the 2004 Microsoft Decision, though slightly reduced the amount of the penalty payment from 899 million euro to 860 million euro. (Judgment of 27 June 2012, *Microsoft v Commission*, T-167/08, ECR, ECLI:EU:T:2012:323)

<sup>3</sup> Detailed facts of this case see Case COMP/C-3/37.792 *Microsoft*, Commission Decision of 24 March 2004. ('Microsoft Decision')

<sup>4</sup> *ibid*, Para 428-464.

connections between PC operating system and server operating system rather than the better quality of its server software.

Realising that it was not possible to expect Microsoft to offer commitments to settle the case, the Commission turned to adopt a prohibition decision, which was considered to be “best for the competition and the consumers in Europe” by creating a strong precedent for the information and communication technology sector.<sup>5</sup> On 24 March 2004, the Commission in its decision found that Microsoft had infringed Article 102 TFEU by “refusing to supply the interoperability information and allow its use for the purpose of developing and distributing workgroup server operating system products from 1998”.<sup>6</sup> Besides a fine of 497.2 million Euros for its infringement of Article 102 TFEU, in the decision the Commission ordered Microsoft to disclose certain specified interoperability information on FRAND terms to any undertaking having an interest in developing and distributing workgroup server operating systems.<sup>7</sup>

Microsoft argued that the ‘exceptional circumstances test’ established in *Magill* should be strictly complied with.<sup>8</sup> As elaborated in the previous chapter, refusal to license IPR by the right holder would constitute abuse under Article 102 TFEU only in exceptional circumstances specified in *Magill* test. The Commission overruled this argument and did not base its decision precisely on the *Magill* test. The Commission denied the “existence of an exhaustive checklist of exceptional circumstances” when evaluating the potential abusive refusal.<sup>9</sup> Instead, the Commission maintained that it would base its decision on a comprehensive examination of the entire circumstances of a specific refusal case.<sup>10</sup> On the one hand, this open-ended approach demonstrates that the Commission was shifting its analytical approach to a more economic and effect-based approach, which afterwards was adopted in the process of modernization of Article 102 TFEU. On the other hand, the legal uncertainty inherently brought about by an open-ended list of exceptional circumstances would make it difficult for the dominant undertakings to *ex ante* estimate the validity of their conducts, since circumstances surrounding

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<sup>5</sup> Speech of Commissioner Monti’s on *Microsoft*, Brussels, 18 March 2004, IP/04/365, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/04/365&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 28 Aug 2011.

<sup>6</sup> Case COMP/C-3/37.792 *Microsoft* Decision, Art. 2(a).

<sup>7</sup> *ibid*, Art. 5.

<sup>8</sup> *ibid*, Para 550-554. It shall be mentioned that the *Microsoft* decision is prior to the *IMS Health* judgment, so only *Magill* test was taken into consideration then.

<sup>9</sup> *ibid*, Para 555.

<sup>10</sup> *ibid*, Para 558.

each specific case could be very different, particularly in different industries; moreover, the adoption of an open-ended list might afford the Commission too much discretion and transform the nature of abusive refusal to license IPR from an exception into a rule.<sup>11</sup>

Regarding the intent to foreclose the downstream market, the Commission maintained that Microsoft was interested in leveraging its dominance on the market for PC operating systems onto the market for workgroup server operating systems since the refusal not only served for the purpose of eliminating the competitors on the downstream market, but also was capable of protecting its dominance from being challenged by the competitors on the market for workgroup server operating systems.<sup>12</sup>

With respect to the new product test, Microsoft argued that the workgroup server systems provided or intended to provide by other vendors were not innovative enough to meet the *Magill* requirement and thereby consumer welfare had not been impaired.<sup>13</sup> The Commission on the one hand indirectly admitted that other non-Microsoft workgroup server systems, even with some added value, competed with Microsoft's product on the same relevant product market.<sup>14</sup> On the other hand, the Commission switched to the negative effects of the refusal on the technical development on the market concerned and consumer harm. If the interoperability information requested had been able to be accessed by the competitors, their products would have been more compatible with Windows PC operating system and accordingly the market for workgroup server systems would have been better developed, which was beneficial to the end users. On the contrary, without adequate interoperability information, the less compatible products provided by the competitors would lead to a loss of users, who were locked in the Microsoft's server system because compatibility with Microsoft's PC operating system was the most important factor when the consumers selected the server systems.<sup>15</sup>

To justify the refusal to share the interoperability information, Microsoft relied on its incentive to invest and innovate. The dominant company argued that the value of the property requested made it different from *Magill* and *IMS Health*. While the interoperability information requested

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<sup>11</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p103.

<sup>12</sup> Case COMP/C-3/37.792 *Microsoft* Decision, *supra* note 3, Para 764-778.

<sup>13</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 621-628.

<sup>14</sup> See e.g. Case COMP/C-3/37.792 *Microsoft* Decision: 'The objective of this Decision is to ensure that Microsoft's competitors can develop products that interoperate with the Windows domain architecture natively supported in the dominant Windows client PC operating system and hence viably compete with Microsoft's work group server operating system.' (Para 1003)

<sup>15</sup> *ibid*, Para 694-701.

was the result of its enormous and continuous intellectual effort, the programme listing information in *Magill* and the ‘1860 brick structure’ in *IMS Health* were acquired with relatively little efforts.<sup>16</sup> What’s more, the interoperability information in *Microsoft* was valuable for the development of related markets because it solved “complex technical challenges”, but not because of other factors, for instance, the participation of the consumers in the creation of the brick structure in *IMS Health*.<sup>17</sup> It is doubted to be unfair if the competition authorities adhere to a *one-size-fits-all* standard and fail to take into account of huge difference in the amount of previous investment and intellectual effort among different cases.<sup>18</sup> If so, in the long run the dominant undertakings would be chilled if their properties might be easily accessed, even with a reasonable loyalty fee in return.<sup>19</sup> On Microsoft’s incentive to invest defence, the Commission adopted a freestyle balancing approach, which compared the negative effects on the incentive of the dominant undertaking brought about by an order to license and the positive impact thereof on competition.<sup>20</sup> By applying such a new balancing approach, the Commission concluded that Microsoft’s future incentive to innovate would not be negatively affected; on the contrary it would be positively inspired if the interoperability information could be accessed by its competitors.<sup>21</sup>

## 2. Contribution of the General Court to the ‘exceptional circumstances test’

Microsoft appealed the 2004 Commission decision before the General Court, which on 17 September 2007 issued its ruling confirming almost all the Commission’s finding and upholding the Commission’s decision except the appointment of a monitoring trustee. The General Court found that the Commission had evidence for its finding that the refusal to supply interoperability information would prevent the competitors from “developing the advanced features of their own products available in the web of interoperability relationships that

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<sup>16</sup> Microsoft claimed that it had invested billions of dollars in software features, functions and technologies. See Case COMP/C-3/37.792 *Microsoft* Decision, Para 709.

<sup>17</sup> James Killick, ‘*IMS and Microsoft* Judged in the Cold Light of *IMS*’ (2004) 1(2) *The Competition Law Review* 23, pp.33-34.

<sup>18</sup> Carsten Reimann, ‘Essential function vs essential facility: defining the amount of R&D protection in high-tech industries after *IMS* and *Microsoft*’, (2004) 1(2) *Competition Law Review* 49, pp.60-61.

<sup>19</sup> James Killick, ‘*IMS and Microsoft* Judged in the Cold Light of *IMS*’ (2004) 1(2) *The Competition Law Review* 23, p42.

<sup>20</sup> Carsten Reimann, ‘Essential function vs essential facility: defining the amount of R&D protection in high-tech industries after *IMS* and *Microsoft*’, (2004) 1(2) *Competition Law Review* 49, p63.

<sup>21</sup> Case COMP/C-3/37.792 *Microsoft* Decision, Para 725.

underpin the Windows domain architecture” and evidence for its finding that “the refusal caused prejudice to consumers”.<sup>22</sup> Hence the Court concluded that the Commission’s findings were not manifestly incorrect. However, the Court did not follow the Commission’s open-ended approach.<sup>23</sup> Instead, the Court adhered to the four conditions of the ‘exceptional circumstances test’ established by the Court of Justice in *Magill* and *IMS Health*, and modified the test in certain respects.

## 2.1 Indispensability

In *Bronner* the Court of Justice made it clear that the condition of indispensability requires that it should be undisputed that for the requesting party there is no other available substitutes, including those disadvantageous alternatives; moreover it should be proved that there are “technical, legal or even economic obstacles capable of making it impossible, or even unreasonably difficult, for any other undertaking alone or in cooperation to potentially establish a substitute”.<sup>24</sup> This test at the outset requires that access to the intellectual property requested is the only choice for any existing operator or potential entrant to be a viable competitor. Accordingly, it is an objective test that does not base on the perspective of the requesting party, but on the standpoint of the dominant undertaking that is expected to be aware of what is indispensable in the downstream market.<sup>25</sup> Secondly, indispensability in this context, as other two exceptional circumstances in the ‘exceptional circumstances test’ – elimination of the competition on the downstream market, and novelty of a new/innovative product – is a question of degree. For instance, necessity of the intellectual property requested, to a certain extent, depends on how to interpret the new product condition: if the new product condition is narrowly interpreted as in *Magill* and *IMS Health*, consequently a higher standard of indispensability shall be applied; if the new product condition is extensively interpreted in the sense that a more attractive product with improvements in certain features is sufficient as in *Microsoft* (see the section ‘new product condition’ below), indispensability condition would be fulfilled if the input could increase the appeal of the competitors’ (proposed) products and failure to supply the input would place the competitors at a disadvantage.<sup>26</sup>

Microsoft maintained that information requested was not indispensable for the reason that the

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<sup>22</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 651-656.

<sup>23</sup> *ibid*, Para 332.

<sup>24</sup> Judgment in *Oscar Bronner*, C-7/97, ECLI:EU:C:1998:264, Para 44.

<sup>25</sup> *ibid*, Para 44-46. John Temple Lang, ‘The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner’ (2000) 1 *Journal of Network Industries* 375, p380.

<sup>26</sup> Thomas Eilmansberger, ‘The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after *IMS Health* and *Microsoft*?’ (2005) 16 *King’s College Law Journal* 329, p339.

interoperability between non-Microsoft server systems and Windows client PC system, as well as between non-Microsoft servers and Microsoft servers could be achieved via other different methods other than via disclosure of the communication protocols in question. Though not as ideal as access to the interoperability information directly, by using them it was still possible to achieve the “minimum level of interoperability” which enabled different systems to work together.<sup>27</sup> Microsoft demonstrated the feasibility of these methods in practice with the example of Linux. According to Microsoft, the market share of Linux increased on the market for workgroup server operation systems without the possession of the communication protocols requested in this case.<sup>28</sup> The Commission responded that first of all the significant role itself played by the interoperability information linking the market for PC operating systems and the market for the workgroup server operating systems, and the strong market power of Microsoft on the former market, gave rise to the indispensability of its communication protocols.<sup>29</sup> Then on the test of indispensability the Commission declared that in the first place, the degree of interoperability information disclosed should be to such an extent that is capable of making a competitor be a “viable competitive constraint” rather as a *de minimis* player as claimed by Microsoft.<sup>30</sup> In the second place, the fact that the competitors of Microsoft on the market for workgroup server systems had not yet been entirely eliminated did not indicate that the indispensability condition was not satisfied.<sup>31</sup> In the third place, according to the Commission, the five alternative methods put forward by Microsoft were not viable substitutes.<sup>32</sup>

The General Court agreed with Commission’s finding that indispensability of the interface information was mainly due to Microsoft’s quasi-monopoly position on the market for PC operating systems, which enabled Microsoft to determine the linking rules at the interface of two markets independently of its competitors.<sup>33</sup> The Court supported the Commission that other alternatives were not effective enough to achieve the high degree of interoperability as what could have been reached by the disclosure of the information at issue.<sup>34</sup> According to the Commission and General Court, any possible solution would not be considered as an alternative under Article 102 TFEU as long as they were not as effective and efficient as the

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<sup>27</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 345.

<sup>28</sup> *ibid*, Para 347.

<sup>29</sup> *ibid*, Para 353.

<sup>30</sup> *ibid*, Para 355.

<sup>31</sup> *ibid*, Para 360.

<sup>32</sup> *ibid*, Para 362.

<sup>33</sup> *ibid*, Para 386- 392.

<sup>34</sup> *ibid*, Para 435.

interface information requested.<sup>35</sup> In this regard, it has been contended that, in consideration of the potentially significant impact of a compulsory license on the incentives to invest and to innovate, the Court should have taken a closer look at the possible alternatives.<sup>36</sup>

In determining the degree of interoperability that Microsoft was expected to provide to its competitors, the Commission and the Court did not explicate why they preferred including also the interaction between server-server rather than protecting only server-client interaction.<sup>37</sup> Protection of the server-server interaction implies that even the competition *in* the market and incremental innovation are pursued; while the competition *for* the market and breakthrough innovation are encouraged if the degree of interoperability only requires the server-client interaction.<sup>38</sup> It demonstrates the interventionist stance held by both of the Commission and the Court, by applying a higher standard of interoperability – including the server-client and server-server interaction, accordingly a lower standard of indispensability. However, such a lower standard, which assumes an indispensable input too readily and places the right owner under constant pressure, particularly in the dynamically competitive industries, might be problematic since these industries change quickly and dramatically.<sup>39</sup>

## 2.2 Elimination of the competition on the downstream market

The second cumulative condition in the ‘exceptional circumstances test’ is that the competition on the downstream market is likely to be eliminated due to the refusal to license. Including this condition in the ‘exceptional circumstances test’ on the one hand is argued to be unnecessary since the requirement of this condition, though in different way, has the same effect as the condition of indispensability.<sup>40</sup> If an intellectual property produced on the upstream market, as an input has been acknowledged to be indispensable for the production on the downstream

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<sup>35</sup> Claudia Schmidt and Wolfgang Kerber, ‘Microsoft, refusal to license intellectual property rights, and the incentives balance test of the EU Commission’ (12<sup>th</sup> Annual Conference at the University of Toronto held by the International Society for New Institutional Economics, Toronto, June 2008), available at <http://ssrn.com/abstract=1297939>, last visited on 20 July 2014, p12.

<sup>36</sup> See Arianna Andreangeli, ‘Interoperability as an “essential facility” in the Microsoft case – encouraging competition or stifling innovation’, (2009) 34 *European Law Review* 587, p598.

<sup>37</sup> Pierre Larouche, ‘The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans’ (2009) 75 *Antitrust Law Journal* 933, p943.

<sup>38</sup> *ibid.*

<sup>39</sup> Barry Doherty, ‘Just What are Essential Facilities?’ (2001) 38 *Common Market Law Review* 397, p424. Analysis of the drastic competition in the dynamically competitive industries see *supra* chapter 2, section 5.2.2(2).

<sup>40</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p122. Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), pp.440-442.

market, refusal to grant a license to access to such intellectual property would likely lead to the exclusion of its competitors once the right owner intends to leave himself the downstream market. Therefore, fulfilment of one requirement normally results in the attainment of the other one. On the other hand, these two conditions have slight difference on their focuses.<sup>41</sup> While the indispensability condition focuses on the significance of the necessity of the input itself, the condition of elimination of the competition emphasises the effect of the refusal conduct. The appraisal of the former condition is an assessment without taking the potential abusive conduct into consideration, while apparently the latter is not.

Like the indispensability condition, this condition is also a question of degree. The main issue is how to measure the likelihood of elimination of the competition by the refusal. It may worth exploring the answers to the two sub-questions involved: firstly, how much competition has been immediately eliminated by the refusal to license? Secondly, in the near future how much competition is estimated to be eliminated? It appears that the first question inquires the immediate exclusionary effect of the refusal behaviour on the market, and the second one concerns not only the effect of the refusal on the existing competition constraints, but also its effect on the potential market entrants. Undoubtedly, all the competition has been eliminated if the right owner is the only player on the downstream market after the refusal. The situation of duopoly could also satisfy this condition if there is little effective competition between the two players.<sup>42</sup> What if several competitors still remain on the market after the refusal in question?

An obvious difference between *Microsoft* case and the experience of EU Commission and Court of Justice in previous cases lies in that, either in *Magill* or in *IMS Health* all the effective competition on the downstream market was immediately – instantly or in no longer than a few days – eliminated once the competitors were refused to access to the copyright. It was not possible for *Magill* or *NDC* to continue supplying their competing products on the relevant markets; otherwise they would have infringed relevant IP law at the national level. Neither the existing competitors, nor the potential market entrants, were able to perform as viable competitors because in *Magill* programmes listing information was the unique source and in *IMS Health* the brick structure was the *de facto* standard.

Quite the opposite, Microsoft's refusal to supply adequate interoperability information did not

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<sup>41</sup> Pierre Larouche, 'The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, fn 49.

<sup>42</sup> John Temple Lang, 'The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner' (2000) 1 *Journal of Network Industries* 375, p384.



have such an immediate exclusionary effect to eliminate its competitors in a short period. According to Microsoft, there were still numerous operators on the market for workgroup server operating systems without access to the communication protocols requested.<sup>43</sup> From the perspective of the Commission, the refusal lead to Microsoft's further consolidated market position and placed the competitors at a strong competitive disadvantage, which was considered to be equal to *risk of elimination of competition*.<sup>44</sup> Yet, from the wordings it is evident that a *risk of elimination of competition* is not as stringent as the criterion of *likely to eliminate all competition*, which terminology remained unchanged in previous case law.<sup>45</sup> According to the General Court, firstly, to invoke Article 102 TFEU in refusal to license cases, it is not necessary to wait until there is no more competition left on the market.<sup>46</sup> A likely prediction about the eliminative effect on competition over time would suffice for the competition authorities.<sup>47</sup> It would be too late to restore the competition process if the infringement has not been brought to an end until the completion of elimination of all the competition. The harm to the competition process and the consumers may be irreparable if it is obliged to prove the actual outcomes. Therefore, what matters is not the immediate result, but the causal relation between the refusal conduct and the likelihood of elimination of all effective competition.<sup>48</sup> The different terminologies used by the Commission – *risk of elimination of competition* and *likely to eliminate competition* – have nothing to do with the standard of assessment for this condition.<sup>49</sup> Furthermore, that elimination of all competition, according to the General Court, does not imply that there are no other participants on the market. The existence of several *de minimis* players, who could not be seen as viable competitive constraints,

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<sup>43</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 442.

<sup>44</sup> Case COMP/C-3/37.792 *Microsoft* Decision, Para 589. See also Claudia Schmidt and Wolfgang Kerber, 'Microsoft, refusal to license intellectual property rights, and the incentives balance test of the EU Commission' (12<sup>th</sup> Annual Conference at the University of Toronto held by the International Society for New Institutional Economics, Toronto, June 2008), available at <http://ssrn.com/abstract=1297939>, last visited on 20 July 2014, p13.

<sup>45</sup> E.g. judgment in *Istituto Chemioterapico Italiano S.p.A. and Commercial Solvents Corporation*, 6 and 7-73, ECLI:EU:C:1974:18, Para 25; Judgment in *Centre belge d'études de marché - Tâchémarketing (CBEM) v SA Compagnie luxembourgeoise de télédiffusion (CLT) and Information publicité Benelux (IPB)*, 311/84, ECLI:EU:C:1985:394, Para 27; Judgment in *Magill* ECLI:EU:C:1995:98, Para 55-56; Judgment in *Oscar Bronner* ECLI:EU:C:1998:264, Para 27; Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 37-38.

<sup>46</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 561.

<sup>47</sup> Emil Paulis, 'Abuses of Dominant Position and Monopolization: Conclusions of the Major Debates in the EU and USA', in Abel M. Mateus and Teresa Moreira (eds.) *Competition Law and Economics: Advances in Competition Policy Enforcement in the EU and North America* (Edward Elgar, 2010), p163; Christian Ahlborn and David S. Evans, 'The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe' (2009) 75 *Antitrust Law Journal* 887, p901.

<sup>48</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 563.

<sup>49</sup> *ibid*, Para 561.

cannot refute the conclusion that all effective competition is at risk of being eliminated on the market.<sup>50</sup> The situation for Microsoft was even worse since the artificially low degree of interoperability, with the network effects in the software market, amounted to a significant barrier to entry for its future competitors.<sup>51</sup>

## 2.3 New product condition

### 2.3.1 The ambiguous definition of ‘a new product’

The new product condition, which was firstly established in *Magill*<sup>52</sup> and subsequently confirmed in *IMS Health*<sup>53</sup>, requires that the alleged refusal has the abusive effect of preventing the emergence of a new product for which the consumers have unmet demand. It might be the most controversial criterion in the assessment of a refusal to license. The rationale for imposing the new product condition is not entirely clear and it does not subject to any accepted legal or economic definition.<sup>54</sup> Though the Court of Justice clearly held in *IMS Health* that a “me-too” version<sup>55</sup> of the dominant undertaking’s product is not enough,<sup>56</sup> it is not clear how much degree of innovation represented in a product is required to make it a new product under Article 102 TFEU.

From an economic perspective, the new product condition is considered as “a bad proxy” to assess the anti-competitive effect on the relevant market caused by the refusal at issue since newness is a variable which is difficult to define and quantify in the framework of competition law.<sup>57</sup> If a product is to be seen as a bundle of characteristics to which the consumers attach their preferences, there are two possibilities of a new product: (1) a new product is a product that is entirely different from the existing products by integrating new characteristics or new features; (2) a new product is a product that represents mere improvements of existing products,

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<sup>50</sup> *ibid*, Para 593.

<sup>51</sup> Floris O.W. Vogelaar, ‘The Compulsory Licence of Intellectual Rights under EC Competition Rules: an analysis of the exception to the general rule of ownership immunity from competition rules’, (2009) 6(1) *The Competition Law Review* 117, p134.

<sup>52</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 54.

<sup>53</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 48-49.

<sup>54</sup> Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ 41 (2004) *Common Market Law Review* 1519, p1527 and 1531.

<sup>55</sup> Derek Ridyard, ‘Compulsory Access under EC Competition Law – A New Doctrine of “Convenient Facilities” and the Case for Price Regulation’ (2004) 11 *European Competition Law Review* 669, p669.

<sup>56</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 49.

<sup>57</sup> Francois Leveque, ‘Innovation, Leveraging and Essential Facilities: Interoperability Licensing in the EU Microsoft Case’ (2005) 28(1) *World Competition* 71, p76.

or in other words performs better on one existing characteristic.<sup>58</sup> The former explanation requires that the product potentially offered by the competitors represents breakthrough innovation. Take the ‘smartphone-feature phone’ case already mentioned in the previous chapter as example, smartphones not only provide basic functions as feature phones; moreover, smartphones represent breakthrough innovations in the sense that the subscribers may use smartphones just as personal computers to, for instance, use web browser to search and access to news, send and receive emails, take photos, download applications, play media documents and find optimum route in GPS system. Therefore, innovation brought about by smartphones in the mobile phone market could satisfy certain unmet consumer demand and thus be considered a new product compared to feature phones. The latter explanation intends to protect value-added competition such as competition on the basis of product quality. A car with max speed of 300 km/h thus might, under this lower standard, be construed as an example of a new product compared to another car with max speed of 200 km/h. Both the Court and its Advocate General in *Magill/IMS Health* leaned towards the former explanation.<sup>59</sup> Another reason for accusing the new product condition of being a bad proxy is that the condition only covers the intent of the competitors and the very preliminary stages of their innovation, which makes the reaction from the consumers and the improvement of the market very uncertain.<sup>60</sup>

Additionally, there are divergent opinions on whether this condition requires a new product to compete with existing products on the same market. According to the Advocate General Gulmann in *Magill*, a new product shall not previously exist on the relevant market and *not compete* with the product already offered by the IPR holder; otherwise, the protection of IPR holder’s innovative effort would be impaired.<sup>61</sup> Yet, Advocate General Tizzano in *IMS Health* argued oppositely, suggesting that a new product is a product with different nature while

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<sup>58</sup> Ibid, pp.75-76. See also Damien Geradin, ‘Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court’s Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*’ 41 (2004) *Common Market Law Review* 1519, p1531; Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla,, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, pp.46-47.

<sup>59</sup> Thomas Eilmansberger, ‘How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses’ (2005) 42 *Common Market Law Review* 129, p159. See also Thomas Eilmansberger, ‘The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after *IMS Health* and *Microsoft*?’ (2005) 16 *King's College Law Journal* 329, p333.

<sup>60</sup> Francois Leveque, ‘Innovation, Leveraging and Essential Facilities: Interoperability Licensing in the EU *Microsoft* Case’ (2005) 28(1) *World Competition* 71, pp.75-76.

<sup>61</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Opinion of Advocate General Gulmann, Para 93, 96 and 97.

competing with existing products.<sup>62</sup> An innovative new product that is capable of creating a *potential downstream market*, as analysed in the previous chapter, may be an appropriate situation where the new product would not compete with existing product offered by the incumbent; without the capability of opening up a new market, new products even those representing breakthrough innovations would remain in the original market and compete with existing products. As illustrated in the table 3 below, nearly half feature phone owners chose smartphone as their new communication devices, while the other half subscribers still confined their choice among the feature phones when they decided to acquire a new mobile phone. Though integrating many new features, it appears from the demand-side smartphones are competing with feature phones for the same group of consumers.

Table 3: smartphone adoption among feature phone owners<sup>63</sup>

Smartphone and Feature Phone Acquisition in Past Month 3 month avg. ending Apr. 2012 Total U.S. Mobile Subscribers, Age 13+ that Acquired Device in Month*			
	Apr-11	Apr-12	Point Change
	38.0%	47.5%	+9.5
Feature Phone to Smartphone	38.0%	47.5%	+9.5
Feature Phone to Feature Phone	60.6%	50.7%	-9.9
N/A**	1.4%	1.9%	+0.5

Compared to the breakthrough innovations, a new product with incremental innovations is more likely to compete on the same market with existing products. Back to *Magill*, Magill combined the information of existing weekly TV guides into its comprehensive product. It was indeed to the benefit of the TV viewers by offering them another option. However, this

<sup>62</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Opinion of AG Tizzano, Para 62, 90(1).

<sup>63</sup> Source from analyst firm comScore's website, available at [http://www.comscore.com/Insights/Press\\_Releases/2012/7/The\\_Great\\_American\\_Smartphone\\_Migration](http://www.comscore.com/Insights/Press_Releases/2012/7/The_Great_American_Smartphone_Migration), last visited on 4 Feb 2013. \*Acquired phone in month refers to people who received a new phone during the month including people who purchased a device, who received a phone but did not directly purchase the device, etc; \*\*N/A refers to mobile subscribers that acquired a new device within the month, but acquired device type was unknown.

comprehensive TV guide was not the result of massive investment and innovative effort. One could also obtain all the same programme information by purchasing several existing TV guides, though it would certainly cost more and cause inconvenience for the consumers.<sup>64</sup> Namely, Magill's new product, if allowed to produce, was still on the same relevant market competing with these TV guides.

### 2.3.2 Extensive interpretation

The unclear interpretation of new product condition has become even more complicated since the General Court in *Microsoft* and the Commission in its Commission Guidance (first in Discussion Paper), deviating from the new product requirement adopted in *Magill/IMS Health*, added follow-on innovation into the 'exceptional circumstances test' and replaced the new product condition by a broader notion of *consumer harm*.<sup>65</sup>

Prior to the *Microsoft* judgment, the Discussion Paper already proposed to introduce the concept 'follow-on innovation', which undermines the original new product condition. It has been criticised that almost all the technologies could, slightly or significantly, be improved by the follow-on innovative activities. If these activities could qualify as follow-on innovation, the new product condition would be satisfied automatically in the sectors involving technologies and dominant firms would then be forced to license their IPR to the competitors.<sup>66</sup>

The General Court in *Microsoft* considered that the conditions in the 'exceptional circumstances test' were not exhaustive, asserting that the prevention of the appearance of a new product in refusal to license cases might merely be one *example* of possible criteria to determine whether the refusal may cause disadvantages for the customers. Such a prejudice might also be caused by the impediment of technical development.<sup>67</sup> The General Court

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<sup>64</sup> Considering the licensing cost paying to IPR holders into account, the price of the comprehensive weekly TV guide could be expected to be much higher than a single weekly TV guide, but may be lower than the total amount of several single weekly TV guides.

<sup>65</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 643-665; DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses. (Hereinafter 'Discussion Paper'), available at <http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf>, last visited on 10 Sep 2011, Para 237-240; Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, [2009] OJ C45/7 (Hereinafter 'Commission Guidance'), Para 86-88.

<sup>66</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, 'DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries' <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, p49.

<sup>67</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 647. See also Pierre Larouche, 'The

maintained that Article 102 TFEU would be infringed not only by practices which prejudice consumers directly, but also by those which indirectly harm their interests.<sup>68</sup> On the one hand, a large group of consumers of Microsoft were locked into Microsoft products owing to the lack of interoperability;<sup>69</sup> on the other hand, the advantage that Microsoft retained discouraged its competitors from developing and marketing workgroup server systems, which ultimately would force other non-Microsoft users to switch to Microsoft.<sup>70</sup> Therefore, such a limitation on technical development of the entire industry deriving from the dominant undertaking's refusal is also within the meaning of Article 102 TFEU. The broader interpretation in *Microsoft* by the General Court, may be due to the facts that: (1) defining precisely the threshold of being a new product is problematic in practice;<sup>71</sup> (2) Microsoft disrupted prior levels of supply and entered into the workgroup server system market, rather than refused to start to supply, which gave rise to that (3) the rivals were not capable of demonstrating their ability to create new products with breakthrough innovations but merely being able to provide value-added competition on the basis of product quality if the interoperability information could be accessed;<sup>72</sup> (4) the characteristic of interoperability information determines that the products offered by the competitors directly compete with the product offered by Microsoft.

Following the Court's judgment, the Commission Guidance introduces a much broader concept *consumer harm* to replace the new product condition. The Commission Guidance seemingly includes two different interpretations of the new product condition - the original new product condition and the *follow-on innovation* condition - by stating:

“The Commission considers that consumer harm may, for instance, arise where the competitors that the dominant undertaking forecloses are, as a result of the refusal, prevented from bringing innovative goods or services to market and/or where follow-on innovation is likely to be stifled. This may be particularly the case if the undertaking which requests supply does not intend to limit itself essentially to duplicating the goods or services already offered by the dominant undertaking on the downstream market, but intends to produce new or improved goods or services for which there is a potential consumer demand or is likely to

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European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, p945.

<sup>68</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 664.

<sup>69</sup> *ibid*, Para 650-651.

<sup>70</sup> *ibid*, Para 653.

<sup>71</sup> See Damien Geradin, 'Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court's Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*' 41 (2004) *Common Market Law Review* 1519, pp.1537-1539.

<sup>72</sup> *ibid*, pp.1533-1536, 1538.

contribute to technical development.”<sup>73</sup>

The original interpretation of the new product condition, which imposes a higher standard burden of proof on the competition authorities, aims to protect the legitimate exercise of IPR held by a dominant undertaking so as to reward its previous innovatory efforts. It requires proof of novelty of the new product and evidence of unmet consumer demand, making the refusal behaviour abusive only in exceptional situations. Nevertheless, the practical difficulty of such an interpretation has given way to the extensive interpretation of the new product condition. The extensive interpretation is based on the belief that consumer welfare is the ultimate objective and it would be better served by protecting competition for innovations, especially in the dynamically competitive industries. From this point of view, this broader interpretation may be positively assessed.<sup>74</sup>

However, the burden of proof in this extensive interpretation is much lower than the narrow one. According to the follow-on innovation approach, it is sufficient for the competitors to demonstrate their “intellectual and financial resources to develop the market in some way”<sup>75</sup> and some “degree of novelty of a product which the competitor was not yet in a position to produce”.<sup>76</sup> It might be even not necessary to define the proposed product in detail which the technology development would bring about.<sup>77</sup> If the technology development is very likely once the essential IPR were accessible for the requesting rivals, the dominant firm may not be able to unilaterally turn down the request. Then this test would be apparently satisfied in almost every IPR case – it goes without saying that the essential technology information disclosed from a dominant undertaking on the market would be valuable for its competitors, directly or indirectly, to improve their competing products.<sup>78</sup> The aim of Article 102 TFEU, which should

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<sup>73</sup> Commission Guidance, *supra* note 65, Para 87.

<sup>74</sup> Claudia Schmidt and Wolfgang Kerber, ‘Microsoft, refusal to license intellectual property rights, and the incentives balance test of the EU Commission’ (12<sup>th</sup> Annual Conference at the University of Toronto held by the International Society for New Institutional Economics, Toronto, June 2008), available at <http://ssrn.com/abstract=1297939>, last visited on 20 July 2014, p14.

<sup>75</sup> Ekaterina Rouseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

<sup>76</sup> John Temple Lang, ‘Mandating access: the principles and the problems in Intellectual Property and competition policy’, (2004) 15(5) *European Business Law Review* 1087, p1111.

<sup>77</sup> Ekaterina Rouseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123; Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p902.

<sup>78</sup> See e.g. James Killick, ‘IMS and Microsoft Judged in the Cold Light of IMS’ (2004) 1(2) *The Competition Law Review* 23, p43; Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p914.

be always borne in mind, is to protect the competitive process and consumer welfare. But it seems that the new product approach has been construed by EU Courts as safeguarding the right of the competitors to compete on a level playing field rather than preventing harm to competition.<sup>79</sup> If the condition could be satisfied too easily, a dominant undertaking would be reluctant to invest in R&D so as to avoid the potential free riding by the competitors. The judgment of the *Microsoft* case implies that the right to refuse would thus become an exception rather than a rule.<sup>80</sup> Thus the right to refuse to grant a license could be claimed only when the requesting parties' intention to develop the market would be highly unlikely achieved.<sup>81</sup> Consequently, in the long run both the entire industry and the consumer welfare would be impaired. Yet, the cases involving copyrights may be relatively less affected by this lower standard than patent cases, since the indispensability condition is difficult to pass in cases involving copyrights.<sup>82</sup> For example, the copyright of Stephen King's book is indispensable for making a movie based on the novel; however, unlike the situation in *Magill* or *IMS Health*, for other movies in the movie making market Stephen King's copyright is obvious not the input required.

## 2.4 Absence of objective justification

### 2.4.1 Introduction

Unlike Article 101 TFEU, under Article 102 TFEU there is no provision to exempt the prosecuted abuse of dominant position. Notwithstanding this, the concept of objective justification has been developed, "on an *ad hoc* basis",<sup>83</sup> by the EU Courts to distinguish legitimate conducts from the abusive ones in the application of Article 102 TFEU.<sup>84</sup> After this

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<sup>79</sup> Damien Geradin, 'Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court's Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*' 41 (2004) *Common Market Law Review* 1519, p1532.

<sup>80</sup> On this point see also Ian S. Forrester, 'Magill Revisited', in Inge Govaere, Reinhard Quick and Marco Bronckers (eds.), *Trade and Competition law in the EU and Beyond* (Edward Elgar, 2011) 376, p388: "In less than 20 years, we have moved from anything being surprising (*Magill*) to everything being possible (*Microsoft*).” See also Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

<sup>81</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

<sup>82</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, 'DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries', available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, pp.47-48.

<sup>83</sup> Alvertina Albors-Llorens, 'The Role of Objective Justification and Efficiencies in the Application of Article 82 EC' (2007) 44 *Common Market Law Review* 1727, p1727.

<sup>84</sup> E.g. in Judgment in *Sirena v. Eda*, 40-70, ECLI:EU:C:1971:18, the Court held that setting a high price could constitute abuse of dominant position "if unjustified by any objective criteria" (Para 16-17). In Judgment in *Deutsche Grammophon Gesellschaft mbH v Metro-SB-Großmärkte GmbH & Co. KG*, 78-70, ECLI:EU:C:1971:59,



notion has been incorporated into the analysis of Article 102 cases, a dominant undertaking could generally claim from three respects to justify his behaviour: external reason<sup>85</sup>, commercial reason<sup>86</sup> and efficiency reason<sup>87</sup>. But the exact scope of objective justification still remains vague in the Article 102 enforcement since its development has not produced a systematic approach for assessment. It is particularly unable to predict how this concept will be interpreted by the EU Commission and the Courts in refusal to license cases as in the case law there is no such a case where the dominant undertaking has successfully justified itself. The General Court in *Microsoft* judgment has not improved the situation. Temple Lang put forward a list of possible situations, which could be claimed by a dominant undertaking to justify his refusal: (1) the efficiency of the downstream users would be reduced; (2) the efficiency or value of the facility requested would be reduced; (3) the facility would be used uneconomically; (4) the improvement, expansion or development of the facility would be interfered with by the proposed access; (5) technical, safety, or efficiency standards would be interfered with; (6) there are genuine and objective advantages of vertical or horizontal integration, which could not be achieved by cooperation with its competitors; (7) the requesting party is intellectually, technically, or financially not qualified; (8) there is no spare capacity of the facility.<sup>88</sup> It seems that most of these defences are merely applicable in the cases involving tangible essential facilities such as ferry port; in IPR cases a dominant undertaking may only rely on the reason of efficiency or competitors' qualification in Temple Lang's list. It has been confirmed by both of the EU Commission and the General Court that the mere possession of IPR does not justify

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the Court made a similar conclusion at Para 19. In Judgment of *United Brands* ECLI:EU:C:1978:22, the Court held that it was "necessary to ascertain whether the discontinuance of supplies was justified" (Para 184). Also in Judgment of *Benzine en Petroleum Handelsmaatschappij BV and others*, 77/77, ECLI:EU:C:1978:141, Para 32-34 Judgment in *Ministère public v Jean-Louis Tournier*, 395/87, ECLI:EU:C:1989:319, Para 46; Judgment in *Centre belge d'études de marché - Tâchémarketing (CBEM) v SA Compagnie luxembourgeoise de télédiffusion (CLT) and Information publicité Benelux (IPB)*, 311/84, ECLI:EU:C:1985:394, Para 27; Judgment in *Magill* ECLI:EU:C:1995:98, Para 55; Judgment of 12 December 1991, *Hilti AG v Commission*, T-30/89, ECR, ECLI:EU:T:1991:70, Para 102-119; Judgment of 6 October 1994, *Tetra Pak International SA v Commission*, T-83/91, ECR, ECLI:EU:T:1994:246, Para 115, 136 and 207; Judgment of 7 October 1999, *Irish Sugar plc v Commission*, T-228/97, ECR, ECLI:EU:T:1999:246, Para 167, 188-189 and 218; Judgment in *Portuguese Republic*, C-163/99, ECLI:EU:C:2001:189, Para 53.

<sup>85</sup> i.e. the shortage of supplies see Judgment in *Benzine en Petroleum Handelsmaatschappij BV and others*, 77/77, ECLI:EU:C:1978:141; the protection of product safety and reliability in judgment of 12 December 1991, *Hilti v Commission*, T-30/89, ECR, ECLI:EU:T:1991:70.

<sup>86</sup> i.e. the protection of commercial interests in Judgment in *United Brands* ECLI:EU:C:1978:22, and Judgment of 1 April 1993, *BPB Industries Plc and British Gypsum Ltd v Commission*, T-65/89, ECR, ECLI:EU:T:1993:31.

<sup>87</sup> i.e. the incentive to innovate and to invest in Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289.

<sup>88</sup> John Temple Lang, 'The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner' (2000) 1 *Journal of Network Industries* 375, p386.

unilateral refusal to license.<sup>89</sup> Except that, case law has not provided further guidance on the precise scope of the objective justification.

#### **2.4.2 Inapplicability of objective necessity and meeting competition defence**

Before the modernization process of Article 102 TFEU formally laid down the notion of efficiency defence, objective necessity – the causes representing public interests that are external to the dominant undertakings, and meeting competition defence which protects private interests on the other hand, were two types of justifications upon which the accused undertakings could rely.<sup>90</sup> The following analysis attempts to illustrate that these two forms of justifications, subject to the interpretation in case law, are not applicable in refusal to license cases due to the inherent features of these cases.

Objective necessity is the first type of justifications a dominant undertaking could rely upon to justify its potentially abusive practices. The possible reasons from the perspective of objective necessity, such as product safety and reliability<sup>91</sup> and a crisis affecting the supply in the entire industry<sup>92</sup>, are characterized as external causes to the dominant undertaking. It is to some extent analogous to a third party's action that breaks the chain of causation or *force majeure* that justifies non-fulfilment of a contract in contract law.<sup>93</sup> In the Commission Guidance, the notion of objective necessity substantially remains the same as that of in the Discussion Paper.<sup>94</sup> A dominant undertaking is not expected to, on its own initiative, regard competitors' products as "dangerous or inferior to its own product" and abuse its market power to exclude them.<sup>95</sup> Meeting competition defence – a "loss minimising reaction to competition from others" – is the second type of objective justifications which however has not been admitted by the

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<sup>89</sup> See case Comp/C-3/37.792 *Microsoft* Decision, Para 709-712 and Case T-201/04 *Microsoft I*, Para 690.

<sup>90</sup> Some authors use terminology 'legitimate business behaviour' instead of the category 'meeting competition defence'. See for instance, Tjarda van der Vijver, 'Objective Justification and Article 102 TFEU', (2012) 35(1) *World Competition* 55, p63. It appears that the scope of the former term is much broader than the meeting competition defence, including not only the commercial behaviour in response to action taken by the competitors, but also any active behaviour constituting competition on the merits.

<sup>91</sup> See Judgment of 12 December 1991, *Hilti AG v Commission*, T-30/89, ECR, ECLI:EU:T:1991:70.

<sup>92</sup> See Judgment of *Benzine en Petroleum Handelsmaatschappij BV and others*, 77/77, ECLI:EU:C:1978:141.

<sup>93</sup> Ivo Van Bael and Jean-François Bellis (eds.), *Competition Law of the European Community*, (fourth edition, Kluwer Law International, 2005), p39.

<sup>94</sup> See Commission Guidance, *supra* note 65, Para 29; Discussion Paper, *supra* note 65, Para 80.

<sup>95</sup> See Commission Guidance, *supra* note 65, Para 29. Judgment of 12 December 1991, *Hilti AG v Commission*, T-30/89, ECR, ECLI:EU:T:1991:70, Para 118-119; Judgment in *Tetra Pak International SA v Commission*, ECLI:EU:T:1994:246, Para 83, 84 and 138.

Commission Guidance.<sup>96</sup> An undertaking in the face of actions taken by its competitors is entitled to defend its legitimate commercial interests and thus to adjust its business strategy, such as providing lower prices or better trading terms to customers, to answer the changing competitive conditions.<sup>97</sup>

In general, to invoke objective necessity or the meeting competition defence in Article 102 cases, a genuine test on the intent behind the behaviour of the dominant undertaking and a proportionality test on the potentially abusive practice itself have to be passed.<sup>98</sup> The purpose of the genuine test, according to *United Brands*, is to filter the cases where the authentic intent of the dominant undertaking's potentially abusive practice is to strengthen its dominant position:

“[A]lthough it is true, as the applicant pointed out, that the fact that an undertaking is in a dominant position cannot disentitle it from protecting its own commercial interests if they are attacked and that such an undertaking must be conceded the right to take such reasonable steps as it deems appropriate to protect its said interest, such behaviour cannot be countenanced if its actual purpose is to strengthen this dominant position and abuse it.”<sup>99</sup>

Regarding the way to investigate whether the genuine purpose behind the allegedly abusive conduct is to strengthen the dominant undertaking's position, or the purpose is legitimate such as to protect public interests like product safety or its commercial interests, EU case law has little contribution. In *BP*, the Court offered a favourable ground for the justification based on shortage of supplies without a more expansive explanation. In *Hilti*, the General Court concluded that it could be inferred that the genuine motivation was apparently not to guarantee product safety and reliability because otherwise the dominant undertaking should have reported to the relevant authority and waited for public intervention.<sup>100</sup> The EU Courts did not make a

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<sup>96</sup> Discussion Paper, *supra* note 65, Para 78.

<sup>97</sup> See e.g. Judgment in *United Brands* ECLI:EU:C:1978:22, Para 189-191; Judgment in *BPB Industries Plc and British Gypsum Ltd v Commission*, ECLI:EU:T:1993:31, Para 69; Judgment of 7 October 1999, *Irish Sugar plc v Commission*, T-228/97, ECR, ECLI:EU:T:1999:246, Para 112 ,

<sup>98</sup> Alvertina Albors-Llorens, ‘The Role of Objective Justification and Efficiencies in the Application of Article 82 EC’ (2007) 44 *Common Market Law Review* 1727, pp.1746-1747. Judgment in *United Brands* ECLI:EU:C:1978:22, Para 189-191.

<sup>99</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 189.

<sup>100</sup> Judgment in *Hilti AG v Commission*, ECLI:EU:T:1991:70, Para 115-119. It is claimed to be not impossible to know the real purpose in cases where the dominant undertakings invoke objective necessity pleas because the stated intentions could be checked against the circumstances of the cases. See Tjarda van der Vijver, ‘Objective Justification and Article 102 TFEU’, (2012) 35(1) *World Competition* 55, p71.

step further on the genuine test until in *BPB* the Court held that:

“The only important issue is whether, through recourse to methods different from those governing normal competition in products based on traders' performance, the conduct at issue was *intended or likely to affect the structure of a market* where, as a direct result of the presence of the undertaking in question, competition had already been weakened.”<sup>101</sup>

This statement put forward to analyse the genuine reason behind the *prima facie* abusive practice by predicting the future variation of the market structure. It is argued that such a low threshold would find a purpose to strengthen a dominant position nearly automatically.<sup>102</sup> Thus it is formidable for the dominant undertaking to prove that its genuine intent is to protect the public or private interests, particularly in refusal to license cases where the refusal of access to the essential IPR by a market leader would inevitably *affect or likely to affect* the structure of the related market where the dominant undertaking presents.

In terms of the proportionality test, the Court in *United Brands* roughly held that the decision adopted by the dominant undertaking should be proportionate to the competitive threat.<sup>103</sup> Without any detailed analytical techniques for the proportionality test, the Court simply concluded that “[t]he sanction consisting of a refusal to supply by an undertaking in a dominant position was in excess of what might, if such a situation were to arise, reasonably be contemplated as a sanction for conduct similar to that for which UBC blamed Oelesen.”<sup>104</sup> There has not been much guidance provided in cases concerning the objective necessity of potentially abusive behaviour, nor in other meeting competition defence cases. Against the background of scant guidance provided in the case law, the Discussion Paper provides that the response of the dominant undertaking shall strictly comply with the principle of proportionality in three respects: “suitable”, “indispensable” and “proportionate”.<sup>105</sup> However, the third prong, which requires protecting the consumer welfare by weighing the interests of the dominant

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<sup>101</sup> Judgment in *BPB Industries Plc and British Gypsum Ltd v Commission*, ECLI:EU:T:1993:31, Para 118. (emphasis added)

<sup>102</sup> Alvertina Albors-Llorens, ‘The Role of Objective Justification and Efficiencies in the Application of Article 82 EC’ (2007) 44 *Common Market Law Review* 1727, pp.1744-1745.

<sup>103</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 190.

<sup>104</sup> *Ibid*, Para 189-191. (emphasis added)

<sup>105</sup> Discussion Paper, *supra* note 65, Para 82. It is worth noting that Advocate General Jacobs in his opinion of case *syfait* (judgment in *syfait v. Glaxosmithkline*, C-53/03, ECLI:EU:C:2005:333), based on the specific feature of the pharmaceutical market, proposed a simpler proportionality test which merely requires that the action of the dominant undertaking cause less harm to the distortion of competition; however, his opinion has been criticised on the grounds that it neglected the objective of the protection of the single market.

undertaking and the interests of its competitors on a case-by-case basis, is argued to be a herculean task for the dominant undertaking.<sup>106</sup> Despite that difficulty, proportionality test should also be flexibly construed to adapt the specific dominance degree in each case.<sup>107</sup>

To sum up, an accused dominant undertaking is highly unlikely to apply the objective necessity or meeting competition defence to justify its potentially abusive refusal to license. For one thing, if the dominant undertaking attempts to demonstrate its refusal is objectively necessary, according to case law the undertaking is not allowed to adopt refusal behaviour on its own initiative before it refers the concerns to relevant authority.<sup>108</sup> For another, the meeting competition defence is not applicable in refusal cases on the grounds that firstly it is almost impossible to pass the genuine test to demonstrate its purpose is not to strengthen the position of dominance, and the proportionality test as well; secondly, this defence is only applicable in otherwise pricing-related abusive conducts, but not in non-pricing related conducts like refusal to supply or refusal to license;<sup>109</sup> thirdly, even this defence could be applied in non-pricing related conducts, according to *United Brands*, a refusal to deal as a form of commercial reaction taken by the dominant undertaking is beyond what is necessary to defend its legitimate commercial interests, since it would highly likely further damage the previously weakened competitive condition prior to the refusal behaviour.<sup>110</sup>

### 2.4.3 Efficiency defence

Prior to the Discussion Paper and Commission Guidance, like what has been done by the US court,<sup>111</sup> efficiency as a possible justification applicable in the framework of Article 102 was

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<sup>106</sup> Alvertina Albors-Llorens, 'The Role of Objective Justification and Efficiencies in the Application of Article 82 EC' (2007) 44 *Common Market Law Review* 1727, p1758.

<sup>107</sup> Tjarda van der Vijver, 'Objective Justification and Article 102 TFEU', (2012) 35(1) *World Competition* 55, p72.

<sup>108</sup> However, there is also an opposite opinion arguing that the dominant undertakings should not be barred from taking actions, *inter alia* offering a higher safety or health standard, on their own initiative to protect public interests particularly when the reaction from the government is not effective and timely. See Tjarda van der Vijver, 'Objective Justification and Article 102 TFEU', (2012) 35(1) *World Competition* 55, p66.

<sup>109</sup> See Discussion Paper, *supra* note 65, Para 81. For an overview of the proper way to apply meeting competition defence in pricing-related conducts (i.e. price cut) see, for example, Donald Slater and Denis Waelbroeck, 'Meeting Competition: Why it is an abuse under Article 82', in Paul Demaret, Inge Govaere and Dominik Hanf (eds.) *30 Years of European Legal Studies at the College of Europe* (P.I.E. Peter Lang, 2005) 431. However, the Discussion Paper in Para 234 surprisingly considers that an objective justification for a refusal to start supplying could be that an undertaking seeking access is not able to prove the appropriate commercial assurances that it will fulfil its obligations.

<sup>110</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 191.

<sup>111</sup> i.e. *Aspen Highlands Skiing Corp. v. Aspen Skiing Co.*, 472 U.S. 585 (1985). In *Aspen*, the Supreme Court held

already taken into account by EU Courts in the assessment of otherwise abusive practices.<sup>112</sup> The Commission, after its efforts incorporating efficiency effects in the modernization of Article 101 TFEU and merger conducts, formally and finally lays down this notion as a possible defence for accused undertakings in its Commission Guidance. In general, the Commission Guidance provides that a dominant undertaking's *prima facie* abusive conduct could be justified when the dominant undertaking is capable of demonstrating the following cumulative conditions:

- (a) The efficiencies are realized or likely to be realized as a result of the conduct concerned;
- (b) The conduct concerned is indispensable to realize these efficiencies;
- (c) The efficiencies outweigh any likely negative effect on competition and consumer welfare;
- (d) The conduct does not eliminate effective competition by removing all or most existing sources of actual or potential competition.<sup>113</sup>

These conditions mirror those of the efficiency defence under Article 101(3) TFEU. According to the first condition, the efficiency gained – such as technical improvements or cost reduction – must directly attribute to the exclusionary conduct. The second condition requires the conduct be indispensable to realise such efficiencies. As the way to interpret indispensability condition in the ‘exceptional circumstances test’, the concept *indispensability* shall be construed as a proportionality filter, requiring that “there are no other economically practicable and less anti-competitive alternatives to achieve the same efficiencies”.<sup>114</sup> These two *indispensability* tests, however, are distinct in the substance. The one in the ‘exceptional circumstances test’ requires *the competition authorities* to examine whether there are any practical alternatives except compelling the dominant undertaking to license its essential IPR, while the indispensability condition in the efficiencies defence imposes the burden of proof on *the*

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that a monopolist may sometimes refuse to share its property if an efficiency justification could be offered (p608).

<sup>112</sup> See e.g. Judgment in *Hoffmann-La Roche*, 85/76, ECLI:EU:C:1979:36, Para 90; Judgment in *Nederlandsche Banden Industrie Michelin*, 322/81, ECLI:EU:C:1983:313 (*‘Michelin I’*), Para 85; Judgment in *Irish Sugar*, T-228/97, ECLI:EU:T:1999:246, Para 189; Judgment of 30 September 2003, *Michelin v Commission*, T-203/01, ECR, ECLI:EU:T:2003:250 (*‘Michelin II’*), Para 59; Judgment of 17 December 2003, *British Airways v Commission*, T-219/99, ECR, ECLI:EU:T:2003:343, Para 280. It is also worth noting that the former Director General of DG Competition Philip Lowe in a speech, which has no legal value though, included efficiency considerations as one of the three types of objective justifications, see Philip Lowe, ‘DG’s Competition’s Review of the Policy on Abuse of Dominance’ in Barry E. Hawk (ed.) *International Antitrust & Policy: Fordham Corporate Law 2003* (Juris Publishing, 2004) 170, pp.170-171.

<sup>113</sup> Commission Guidance, *supra* note 65, Para 30.

<sup>114</sup> Discussion Paper, *supra* note 65, Para 86.

*dominant undertaking*, who should provide convincing evidence to demonstrate that its refusal conduct is the optimal choice. Another point of dissimilarity is that, according to the Discussion Paper, the dominant undertaking only needs to consider “realistic and attainable alternatives”, without taking into account other “hypothetical or theoretical” options.<sup>115</sup>

The third condition requires that the net effect brought about by the conduct shall be positive, in other words, the efficiencies gained must outweigh the negative effect on competition. The net effect of a *prima facie* abusive conduct could be indicated by its impact on consumer welfare. It is asserted by the Discussion Paper that a plea based on efficiencies would be untenable if such alleged efficiencies cannot pass-on to the consumer and compensate them for any actual or likely harm caused by the conduct.<sup>116</sup> Though the pass-on requirement is not explicitly stated in the Commission Guidance (Para 30), it could still be inferred, reading together with the Commission’s balancing test (Para 31) where the consumer welfare is the benchmark, that consumers should benefit from the efficiency gained since otherwise the proposed efficiency is unlikely to outweigh the consumer harm caused by the *prima facie* abusive conduct.<sup>117</sup> Additionally, compared to the negative impact upon the consumers, the efficiencies shall be realized and benefit consumers timely. The later the efficiencies are delivered to the consumers, the less the efficiencies would be valued.<sup>118</sup>

The fourth condition emphasises the significance of preserving the competitive process in the marketplace. Even though other three prongs have been proved by the dominant undertaking in a specific case, efficiency defence would not be successfully invoked as long as all or most effective competition on the relevant market has been removed. It is based on the belief that the incentive of the dominant undertaking to pass the efficiencies onto the consumers remains questionable if there is no competition pressure on the market.<sup>119</sup> It is the rivalry and the competitive process that are the very essence protected by the competition authorities, but not the possible efficiencies.<sup>120</sup> However, this provision is argued to have deviated from the general trend in Article 102 modernization in the sense that it places the protection of competitive process above ultimate consumer welfare.<sup>121</sup>

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<sup>115</sup> *ibid.*

<sup>116</sup> *ibid.*, Para 88.

<sup>117</sup> See Anne C. Witt, ‘The Commission’s Guidance Paper on Abusive Exclusionary Conduct – More radical than it appears?’ (2010) 35 *European Law Review* 214, pp.229-230.

<sup>118</sup> Discussion Paper, *supra* note 65, Para 89.

<sup>119</sup> *Ibid.*, Para 90.

<sup>120</sup> *Ibid.*, Para 91.

<sup>121</sup> Alvertina Albors-Llorens, ‘The Role of Objective Justification and Efficiencies in the Application of Article 82

Although the Commission Guidance makes an efficiency defence available for dominant undertakings, it does not make Article 102 TFEU more lenient than before. After the undertaking's defence the ultimate measurement is at the discretion of the Commission. It is a formidable task for the accused dominant undertaking to, at the end of the analysis, convince the competition authority, who is already satisfied with its *prima facie* finding of the conduct's anti-competitive effects, to accept the counterargument on the conduct's positive effects.<sup>122</sup> The competition authorities in practice may make errors and end up establishing abuses even when the conducts at issue are pro-competitive due to the discretion inherent in any balancing.<sup>123</sup>

The doubts have been raised on the practical worth of the efficiency defence on the ground that that an overwhelming burden of proof is imposed upon a dominant undertaking to apply this justification.<sup>124</sup> The dominant undertaking concerned may particularly struggle to prove remaining effective competition and its willingness to pass the efficiencies to the consumers. On the one hand, prior to the justification stage, the likely elimination of effective competition on the downstream market, which is required by the 'exceptional circumstances test', has already been demonstrated by the competition authorities in establishing a *prima facie* abuse. This is more obvious in refusal to license cases where the refusal conduct at issue would by and large lead to the elimination of effective competition without even generating detriment to consumers.<sup>125</sup> On the other hand, this efficiencies defence requests exactly the very opposite fact that the competition on the relevant market would not be removed. It seems that unless the competition authority makes an error in its assessment on the remaining competition on the market, otherwise the dominant undertaking cannot justify its conduct. A possible explanation for this contradiction might be that different degrees shall be included into consideration in

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EC' (2007) 44 *Common Market Law Review* 1727, p1759.

<sup>122</sup> Pierre Larouche, 'The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, p948. Arianna Andreangeli, 'Interoperability as an "essential facility" in the Microsoft case – encouraging competition or stifling innovation', (2009) 34 *European Law Review* 587, p602.

<sup>123</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p599; Damien Geradin, 'Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court's Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*' (2004) 41 *Common Market Law Review* 1519, pp.1939-1943.

<sup>124</sup> Alvertina Albors-Llorens, 'The Role of Objective Justification and Efficiencies in the Application of Article 82 EC' (2007) 44 *Common Market Law Review* 1727, p1759.

<sup>125</sup> See Massimo Motta, 'The European Commission's Guidance Communication on article 82', (2009) 30(12) *European Competition Law Review* 593, p598.



assessing the elimination of effective competition respectively in the ‘exceptional circumstances test’ and in the efficiency defence.<sup>126</sup> That is to say, the remaining competitors left on the relevant market might be optimistically regarded as viable competition constraints in the efficiency defence, while the same remaining competition is pessimistically considered to be not capable of exerting competition pressure on the dominant undertaking from the perspective of the Commission when applying the ‘exceptional circumstances test’.

For the dominant undertakings with a monopoly level of market power, or known as ‘super dominance’, according to the Commission, it is highly unlikely that such an undertaking is capable of demonstrating its incentive to deliver the efficiencies to consumers because of the insufficient remaining competitive pressure.<sup>127</sup> Generally speaking, possession of a market share of 75%, according to the Commission, indicates that a dominant undertaking has a market position approaching that of a monopoly market power.<sup>128</sup> It is in accord with the Advocate General Fennelly’s opinion in *Compagnie Maritime Belge*, arguing that an undertaking holding a super dominant position deserves particularly close scrutiny.<sup>129</sup> Accordingly, it could be imagined that the efficiency defence would not have been successfully invoked in *Magill*, *IMS Health* and *Microsoft* where their dominant positions were so strong that the efficiencies gained (if any) would not be passed to consumers and the competition on the downstream market was highly likely to be eliminated. The defence is therefore expected to only succeed in cases where a dominant undertaking has a relatively weak dominant position and there are effective competition constraints from actual or potential competitors. Yet, it is argued that whether the efficiency claim can be accepted should be subject to a comprehensive assessment of the entire circumstances surrounding a given case, including the dominance degree of the incumbent; it seems not compatible with the effect-based approach if it is explicitly stated, “as a matter of principle”, that dominant undertakings with monopoly market power are highly unlikely to invoke the efficiency defence.<sup>130</sup>

With respect to the specific forms of abusive conducts, the Commission Guidance considers two examples of efficiencies in refusal behaviour in particular, on which a dominant undertaking could rely. One relates to reaping a sufficient return on the dominant undertaking’s

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<sup>126</sup> See Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010) p383.

<sup>127</sup> See Commission Guidance, *supra* note 65, Para 30; Discussion Paper, *supra* note 65, Para 90.

<sup>128</sup> See Discussion Paper, *supra* note 65, Para 92.

<sup>129</sup> Judgment in *Compagnie Maritime Belge Transports SA v. Commission*, C-395/96 P and C-396/96 P, ECLI:EU:C:2000:132, Opinion of Advocate General Fennelly, Para 136.

<sup>130</sup> Tjarda van der Vijver, ‘Objective Justification and Article 102 TFEU’, (2012) 35(1) *World Competition* 55, fn84 at p68.

previously extensive investments, realizing of which would produce incentive to innovate and invest on the part of the dominant undertaking. The dominant undertaking could also claim that its innovation will be negatively affected by either the obligation to license its essential IPR, or the change of market conditions caused by the obligation.<sup>131</sup>

*Microsoft* case demonstrates the Achilles' heel of the efficiency defence: it is difficult to define and quantify the incentive to invest, for both of the dominant undertaking and the competition authorities.<sup>132</sup> The substantial assertion of Microsoft was that an obligation to share its interface information would discourage its incentive to innovate and invest. In *Microsoft* decision, the Commission did not directly balance Microsoft's incentive to innovate, as its efficiency defence, against the anti-competitive effects of the *prima facie* abusive refusal. Instead, the Commission adopted the alleged 'incentive balancing test', which compared Microsoft's incentive to innovate with the incentives to innovate of the entire industry.<sup>133</sup> The basic idea of the novel test is to solve the conflict between the individual economic freedom of the dominant undertaking and the development of the entire industry by weighing the impact of a compulsory licensing on the incentives to innovate both for the dominant undertaking and other players on the market. If the negative impact on the incentive to innovate of the dominant undertaking is outweighed by the positive effect on the incentives of the entire industry, then an order imposed by the competition authority to license IPR would be justified. By doing so, it seems that the Commission converted the initial test – balancing the efficiencies claimed by Microsoft against the exceptional circumstances – into a novel incentive balancing test.<sup>134</sup> However, the incentive balancing test bases neither on any previous case law, nor on any Commission decision. There are divergent opinions on this test between scholars. Proponents welcome this approach, asserting that from an economic view, it is entirely accord with the basic trend of the more economic based approach adopted in European competition policies.<sup>135</sup> Opponents primarily argue on two points: this new balancing test provides insufficient legal

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<sup>131</sup> See Commission Guidance, *supra* note 65, Para 89-90.

<sup>132</sup> See Pierre Larouche, 'The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, p947.

<sup>133</sup> Case COMP/C-3/37.792 *Microsoft* Decision, Para 783.

<sup>134</sup> James Killick, '*IMS* and *Microsoft* Judged in the Cold Light of *IMS*' (2004) 1(2) *The Competition Law Review* 23, pp.37-38.

<sup>135</sup> See e.g. Claudia Schmidt and Wolfgang Kerber, '*Microsoft*, refusal to license intellectual property rights, and the incentives balance test of the EU Commission' (12<sup>th</sup> Annual Conference at the University of Toronto held by the International Society for New Institutional Economics, Toronto, June 2008). Available at SSRN: <http://ssrn.com/abstract=1297939>, last visited on 20 July 2014, p2.

certainty for the dominant undertaking to predict *ex ante*;<sup>136</sup> this modified balancing approach only takes into account dynamic efficiencies, and short-term gains and loss of a proposed compulsory licensing.<sup>137</sup> Regarding this novel balancing test, the General Court maintained that Microsoft's assertion that the Commission applied a new evaluation test was a "misreading" of the decision.<sup>138</sup> The Court held that Microsoft did not manage to invoke the objective justification because its arguments were not concrete. The only certainty is that the mere possession of intellectual property rights cannot in itself constitute objective justification for the refusal to grant a license.<sup>139</sup> The Court did not make in-depth comments on the objective justification but rather avoided the conundrum. The efficiency at stake in *Microsoft* – incentive to innovate, is such a dynamic efficiency (rather than static efficiency) that there might never be any quantified efficiency gained from the refusal.<sup>140</sup> That might explain why the Court was unwilling to be involved in deciding the difficult trade-off between preserving *ex ante* efficiencies by allowing a refusal and promoting *ex post* efficiencies by denying the refusal.<sup>141</sup>

Additionally, with regard to the role played by the scale of the innovator's investment, the view that the size of the previous investments in innovation is a decisive factor in the evaluation of the competition authorities has been criticised on the grounds that: (1) it is not possible, or extremely difficult to identify the cases in which the innovator with a lower investment in research has been excessively rewarded either under the framework of competition law, or in the context of intellectual property law; in other words, it is impractical to set a threshold to distinguish cases with higher investment and those with lower investment; (2) the investment in the intellectual property rights at stake, such as the interoperability information in *Microsoft*, may be difficult to observe, verify and calculate precisely, and separately; (3) the 'higher investment – lower liability' policy might have the effect of encouraging investments on innovative activities on the one hand; but on the other hand it is apparently not the objective pursued by the Article 102 TFEU that giant undertakings with significant financial strength

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<sup>136</sup> James Killick, 'IMS and *Microsoft* Judged in the Cold Light of *IMS*' (2004) 1(2) *The Competition Law Review* 23, p44.

<sup>137</sup> Damien Geradin, 'Limiting the Scope of Article 82 EC: What Can the EU Learn from the U.S. Supreme Court's Judgment in *Trinko* in the Wake of *Microsoft*, *IMS*, and *Deutsche Telekom*' (2004) 41 *Common Market Law Review* 1519, fn76.

<sup>138</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 704.

<sup>139</sup> *Ibid*, Para 690.

<sup>140</sup> Pierre Larouche, 'The European *Microsoft* Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, p947.

<sup>141</sup> Dan Eklof, 'The *Microsoft* Case – at the Heart of the IP/Antitrust Intersection', in Ariel Ezrachi (ed.) *Article 82 EC: Reflections on its Recent Evolution* (Hart Publishing, 2009), p106.

would thus be favoured over small ones.<sup>142</sup>

## 2.5 The aftermath of Microsoft Judgment

### 2.5.1 Refusal to license vs. refusal to supply

Prior to *Microsoft*, the key factor in distinguishing the analytical framework applicable in refusal to license IPR cases from the approach applicable in other refusal cases was whether the emergence of a new product has been prevented by the refusal. However, the relatively looser requirement of the ‘exceptional circumstances test’, *inter alia* the extensive interpretation of the new product condition, has bridged the gap between the approaches towards refusal to license and refusal to supply under EU competition law.<sup>143</sup> While the Discussion Paper has a full section on refusal to license IPR, this equal approach has been reflected in Commission Guidance where refusal to license IPR is subsumed into the general discussion on refusal to deal. It is worth investigating the old, yet still heated debate with opposing arguments: whether refusal to license IPR should be treated in a different way compared to refusal to supply other properties.

The opponents of an equal approach<sup>144</sup> insist that particular care is required when assessing refusal cases involving IPR owing to some unique economic characteristics of IPR:

- (1) Intellectual property is particularly susceptible to free riding compared to tangible property, and this problem could not be completely overcome by legal protection;<sup>145</sup>
- (2) Intellectual property innovators undertake higher sunk costs than that in other forms of investment; even if the R&D could lead to a commercial product on a mass-factory scale, these costs are generally not recoverable;<sup>146</sup>
- (3) Intellectual property not only facilitates the development of its own industry, but also often

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<sup>142</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp's Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, pp.52-54.

<sup>143</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p92.

<sup>144</sup> See for instance John Temple Lang, ‘Anti-Competitive Abuses Under Article 82 Involving Intellectual Property Rights’, in Claus Dieter Ehlermann and Isabela Atanasiu (eds.) *European Competition Law Annual 2003: What is an Abuse of a Dominant?* (Hart Publishing, 2005); James Langenfeld, ‘Intellectual Property and Antitrust: Steps Towards Striking a Balance’ (2001) 52 *Case Western Reserve Law Review* 91.

<sup>145</sup> James Langenfeld, ‘Intellectual Property and Antitrust: Steps towards Striking a Balance’ (2001) 52 *Case Western Reserve Law Review* 91, p93. See also e.g. the 1995 DOJ/FTC Antitrust Guidelines for the Licensing of Intellectual Property, section 2.1: “Intellectual property has important characteristics, such as ease of misappropriation, that distinguish it from many other forms of property”.

<sup>146</sup> James Langenfeld, ‘Intellectual Property and Antitrust: Steps towards Striking a Balance’ (2001) 52 *Case Western Reserve Law Review* 91, pp.93-94.

spills extra social benefits over into other industries. The right holder however may not be able to recoup these spill-over benefits;<sup>147</sup>

(4) Compulsory license would impede innovation in industries where substantial investment is required.<sup>148</sup>

However, another group of commentators maintain that it is not justified to adopt a stricter standard in analysing refusal to license cases.<sup>149</sup> The reasons to support a higher standard of protection for IPR are not so convincing in the following respects. In the first place, the rationales behind protecting the investment in tangible properties and protecting the investment in IPR are essentially the same: all forms of commercial properties, tangible or not, are created by significant investment with investors' hope of certain forms of financial return and the risk of succeeding on the market as well.<sup>150</sup> In the second place, regarding the free riding concern, it is true that intellectual properties are generally less difficult to copy and usually not subject to

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<sup>147</sup> *ibid*, p93.

<sup>148</sup> See e.g. Judgment in *Oscar Bronner* ECLI:EU:C:1998:264, Opinion of AG Jacobs, Para 62. See also Judgment of 26 October 2001, *IMS Health v Commission*, T-184/01 R, ECR, ECLI:EU:T:2001:259, the Order of the President of the General Court, Para 125.

<sup>149</sup> See e.g. Cyril Ritter, 'Refusal to Deal and "Essential Facilities": Does Intellectual Property Require Special Deference Compared to Tangible Property?', (2005) 28(3) *World Competition* 281; Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexl (ed.) *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, p68; Josef Drexl, Beatriz Conde Gallego, Stefan Enchelmaier, Matthias Leistner and Mark-Oliver Mackenrodt, 'Comments of The Max Planck Institute for Intellectual Property, Competition and Tax Law (Munich) on the DG Competition Discussion Paper of December 2005 on the Application of Art. 82 EC to Exclusionary Abuses', (2006) 37 *International Review of Intellectual Property and Competition Law* 558, Para 14; Matthias Leistner, 'Intellectual Property and Competition Law: The European Development from Magill to IMS Health Compared to Recent German and U.S. Case Law' (2005) *ZWeR - Zeitschrift für Wettbewerbsrecht* 138, p150; Einer Elhauge, 'Defining Better Monopolization Standards' (2003) 56 *Stanford Law Review* 253, p276; Donald F. Turner, 'Basic Principles in Formulating Antitrust and Misuse Constraints on the Exploitation of Intellectual Property Rights' (1985) 53 *Antitrust Law Journal* 485, p489; Thomas Eilmansberger, 'How to Distinguish Good From Bad Competition Abuses' (2005) 42 *Common Market Law Review* 129, p158; Andreas Heinemann, 'Compulsory licences and product integration in European competition law – assessment of the European Commission's Microsoft decision', (2005) 36(1) *International Review of Intellectual Property and Competition Law* 63, pp.72-73.

<sup>150</sup> Robert O'Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p421. See also Christophe Humpe and Cyril Ritter, 'Refusal to Deal', (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, pp.143-144; Thomas Eilmansberger, 'How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses' (2005) 42 *Common Market Law Review* 129, p159.

capacity constraints compared to the tangible properties, but for one thing this is the very reason why right holders are granted exclusive rights by IPR laws,<sup>151</sup> for another the vulnerability of IP does not indicate their value is higher than tangible properties.<sup>152</sup> It is not well-grounded that refusal to license should be treated in a “more leniently” way under Art 102 TFEU in order to insure the exclusivity granted by the IPR laws.<sup>153</sup> In the third place, *ex ante* investments in intellectual properties are not always more costly than those in tangible properties, such as investments in infrastructure required for broadband internet access.<sup>154</sup> In the fourth place, on the relation between the degree of protection imposed on IPR and the incentive to innovation, a higher standard of IP protection may not necessarily result in the right holders’ more incentive to innovate,<sup>155</sup> since the degree of IP protection curve and the innovation curve are not indefinitely parallel.<sup>156</sup>

As illustrated in the graph 4 below, the research of Langenfeld demonstrates that with complete IP protection, the number of innovations (the blue curve), as well as the total social welfare (the red curve), is at a relatively low position. The number of innovations increases as the degree of IP protection decreases, and the innovation curve reaches the peak at point A. After that point, the innovation curve descends as the degree of IP protection continues decreasing. It is also worth noting that the total welfare is lower than the number of innovations until the intersection of two curves, right of point A, and the optimal total welfare will be at point B with less IP protection than the optimal innovation position.<sup>157</sup> Therefore, taking into account of the incentive to innovate and the total social welfare, the optimal degree of IP protection will be at

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<sup>151</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), p422.

<sup>152</sup> Thomas Eilmansberger, ‘How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses’ (2005) 42 *Common Market Law Review* 129, p159.

<sup>153</sup> Robert O’Donoghue and A Jorge Padilla, *The Law and Economics of Article 82 EC* (Hart Publishing, 2006), pp.422-423.

<sup>154</sup> *ibid* 423.

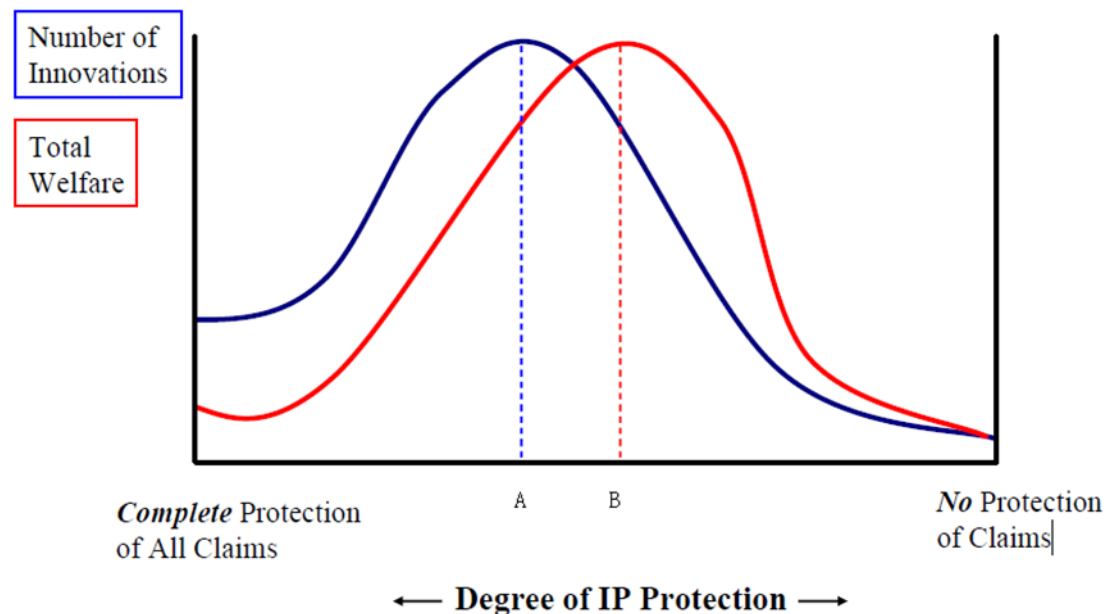
<sup>155</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p145.

<sup>156</sup> *Ibid*, pp.145-46.

<sup>157</sup> See more in James Langenfeld, ‘Intellectual Property and Antitrust: Steps Towards Striking a Balance’ (2001) 52 *Case Western Reserve Law Review* 91, p98. Furthermore, ‘the relationship between consumer surplus and the degree of intellectual property protection would have a similar pattern to the total welfare curve, but optimal consumer welfare will reach its maximum further to the right of B with less intellectual property protection.’ (fn 25 at 98)

a certain position between point A and point B, at the intersection of innovation curve and welfare curve.

Graph 4: optimal IP protection<sup>158</sup>



Moreover, conferring higher protection on intellectual properties might attract the dominant undertakings to “incorporate” their IPRs into other valuable properties in order to obtain a higher protection and thus distort the allocation of business resources.<sup>159</sup> Actually, whether the IPR would be subject to compulsory license is argued to be merely a “negligible” factor as long as the undertakings are “rational”.<sup>160</sup> On the one hand, the Commission held in the *Microsoft* decision that compulsory licensing would not discourage the incentive of a dominant undertaking to innovate and invest.<sup>161</sup> The view that compulsory licensing undermines innovation also ignores *second generation inventions* which may benefit from the duty to share

<sup>158</sup> James Langenfeld, ‘Intellectual Property and Antitrust: Steps Towards Striking a Balance’ (2001) 52 *Case Western Reserve Law Review* 91, p97.

<sup>159</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p144.

<sup>160</sup> Ibid, p146.

<sup>161</sup> COMP/C-3/37.792 *Microsoft* Decision, Para 713-729.

IPR and be developed by actual/potential competitors or the dominant undertakings itself based on the *first generation inventions*.<sup>162</sup> On the other hand, the reasonable loyalty in return for compulsory licensing ensures that there is no financial loss for the IPR holders.

The arguments above both make sense from their corresponding perspectives; however, neither is particularly compelling. It might not be optimal to treat intellectual properties and other tangible properties in such an absolutely equal way that ignores the characteristics of intellectual property – by interpreting the new product condition in an extremely extensive way. On the other hand, interpreting the new product condition in a narrower way seems inconsistent with the current trend of the EU Commission and EU Courts' practice, and requires a precise method to quantify and calculate the newness in a new product, which is the very conundrum in the original new product condition. It remains to be observed in future cases the answer to the question of whether the analytical framework for refusal cases involving IPR will be identical with that for tangible property cases.

### **2.5.2 Microsoft Judgment: progress or retreat?**

In the light of the foregoing analysis, it is manifest that the General Court has adopted weaker criteria in *Microsoft* judgment.<sup>163</sup> Apart from the consequence deriving from the extensive interpretation of the new product condition, commentators have divergent understandings on the implication of the entire judgment.

According to Ahlborn and Evans, the General Court's judgment represents its *ordoliberal* thinking.<sup>164</sup> That is to say, the Court did not take the advantage of this opportunity to transpose the economic and effect-based analysis, which has been already adopted in merger control and Article 101 cases, into exclusionary abusive cases. On the contrary, the Court still relied on a form-based approach and did not emphasize the effects caused by the refusal on consumer welfare.<sup>165</sup> For instance, Ahlborn and Evans argue that, contrary to what maintained by the

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<sup>162</sup> Cyril Ritter, 'Refusal to Deal and "Essential Facilities": Does Intellectual Property Require Special Deference Compared to Tangible Property?' (2005) 28(3) *World Competition* 281, p281; Steven C. Salop and R. Craig Romaine, 'Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft' (1999) 7 *George Mason Law Review* 617, p664.

<sup>163</sup> Christian Ahlborn and David S. Evans, 'The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe' (2009) 75 *Antitrust Law Journal* 887, p889.

<sup>164</sup> *ibid*, p911. For an overview of ordoliberalism, see for example, David J. Gerber, 'Law and Competition in Twentieth Century Europe: Protecting Prometheus', chapter VII 'Ordoliberalism: A New Intellectual Framework for Competition Law' (Oxford University Press, 1998) 232.

<sup>165</sup> Christian Ahlborn and David S. Evans, 'The Microsoft Judgment and Its Implications for Competition Policy



Court, a competitive advantage stemming from better compatibility with other products, as the quality of a product, should also be included in the definition of *competition on the merits*.<sup>166</sup> Therefore, this judgment has been criticized that it will chill the dominant undertakings, who assume that choosing their trading partners is at their own discretion.<sup>167</sup> Furthermore, it is contended that such an interventionist stance in *Microsoft* has been reflected in the Commission Guidance, in particular the seemingly more stringent approach towards the termination of an existing supply relationship.<sup>168</sup> According to the Commission Guidance, the refusal by a dominant undertaking to continue an already existing supply, including the situation involving IPR licensing, would “be more likely to be found to be abusive than a *de novo* refusal to supply”, especially when the input owner could not demonstrate why in the past it was in his interest to supply but it is currently not any more.<sup>169</sup> As a result, it is argued that, the approach in *Microsoft* judgment by the General Court, largely followed by the Commission Guidance, emphasises on the short term impact of refusal to license and thus, would hold back the incentives of all the undertakings on the related market to innovate, particularly in the dynamically competitive industries, in the sense that the resources aiming at creating breakthrough innovations would be diverted onto developing the follow-on and incremental innovations.<sup>170</sup>

However, an opposite opinion has been expressed by Larouche, who regards the impact of *Microsoft* judgment not so negative. According to Larouche, *Microsoft* judgment has made some progress in improving the analytical techniques towards an economic and effect-based approach.<sup>171</sup> Though containing some disadvantages, it would be overstated to tag the General Court’s approach, as held by Ahlborn and Evans, as *ordoliberalism*.<sup>172</sup> On the contrary, the foremost chilling effect of this judgment on the incentive of dominant undertakings to innovate

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Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, pp.889 and 927.

<sup>166</sup> *ibid*, pp.912-913. Opposite opinion see, for example, Pierre Larouche, ‘The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans’ (2009) 75 *Antitrust Law Journal* 933, p962.

<sup>167</sup> Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p903.

<sup>168</sup> See Arianna Andreangeli, ‘Interoperability as an “essential facility” in the Microsoft case – encouraging competition or stifling innovation’, (2009) 34 *European Law Review* 587, pp.605-610.

<sup>169</sup> Commission Guidance, *supra* note 65, Para 84.

<sup>170</sup> See Arianna Andreangeli, ‘Interoperability as an “essential facility” in the Microsoft case – encouraging competition or stifling innovation’, (2009) 34 *European Law Review* 587, pp.609-610.

<sup>171</sup> Pierre Larouche, ‘The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans’ (2009) 75 *Antitrust Law Journal* 933, p962.

<sup>172</sup> *ibid*.

is “psychological”,<sup>173</sup> and the likelihood of a compulsory licensing is a negligible factor once the dominant undertakings are rational.<sup>174</sup> On the part of the competition authorities, the triumph in this milestone case has built the confidence of EU Commission and encouraged the competition watchdog to continue inquiring and regulating the high-tech industries through a number of Article 102 cases.<sup>175</sup>

### 3. Other approaches

Apart from the ‘exceptional circumstances test’ developed by the European Courts in case law (the narrow test in *Magill/IMS Health* by the Court of Justice and the extensive one in *Microsoft I* by the General Court), there are several alternative approaches proposed by competition law scholars, aiming at resolving the conundrum at the intersection of competition rules and protection of intellectual property rights.

#### 3.1 Contestable-market theory

The theory of contestable-market was firstly put forward in 1980s.<sup>176</sup> This theory has been developed by Heinemaan to address the competition concern in the refusal to license cases.<sup>177</sup> In consonance with the classification of two-market situations in the previous chapter,<sup>178</sup> Heinemaan proposes a two-fold approach to deal with the delicate relation between the protection of exclusive rights conferred by intellectual property law, and the market contestability required by competition policies.

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<sup>173</sup> *ibid*, 960.

<sup>174</sup> Christophe Humpe and Cyril Ritter, ‘Refusal to Deal’, (2005) GCLC Research Papers on Article 82 EC 07/2005, available at <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>, last visited on 15 March 2012, p146.

<sup>175</sup> Pierre Larouche, ‘The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans’ (2009) 75 *Antitrust Law Journal* 933, p960. These after-Microsoft cases include, for instance, Intel (Case COMP/C-3/37.990), Rambus (Case COMP/C-3/38.636), Qualcomm (Case COMP/C-3/39.247), IBM (Case COMP/39.692), Google (Case COMP/C-3/39.740).

<sup>176</sup> See William J. Baumol, John C. Panzar and Robert D. Willig, *Contestable Markets and the Theory of Industry Structure* (Harcourt College Pub 1988).

<sup>177</sup> Andreas Heinemann, ‘The contestability of IP-protected markets’ in Josef Drexler (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54.

<sup>178</sup> See chapter 2, section 5.1.2.

In the situation of vertically related markets, the protection of intellectual properties covers not only upstream markets, but also certain downstream markets.<sup>179</sup> Stephen King's copyright on his book not only protects his book from being copied without the author's license, but also reserves him the right, for instance, to adapt it into a film. Although it is an open question of whether IPR protection *attributes* the downstream market to the right holder,<sup>180</sup> according to Heinemaan, whether a new product has been suppressed on the downstream market has nothing to do with the evaluation of the potential abusive refusal to license.<sup>181</sup> The right holder is not obliged by the competition law to grant a license for other competitors on the downstream market to access to his intellectual property, since the right holder's innovative efforts is normally covered in the scope of the IPR reward.<sup>182</sup> Nevertheless, such an unlimited right to refuse should not be rewarded in the cases where the IPR requested is the *de facto* industry standard on the market and created by several independent undertakings, since the foreclosure effect on the downstream market due to the collective refusal is much greater than that of in a single undertaking's unilateral refusal.<sup>183</sup>

However, according to Heinemaan, this balancing approach in the vertically related markets might not be applicable in the situation of conglomerate markets where the scope of exclusive rights might not reach the surrounding markets but only cover the centre market.<sup>184</sup> As observed in *Microsoft*, the IPR conferred on the product in the centre market – customer PC operating systems, does not necessarily cover its surrounding markets, for instance the market for workgroup server operating systems. Therefore, it would not be allowed to unduly use an IPR, such as refusal to license in the markets where beyond the boundary of the IPR,

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<sup>179</sup> Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexel (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, p66.

<sup>180</sup> Drexel argues that IPR has largely covered certain downstream market, but not "attributed" the market to the right holder unless the IPR is essential input. See Josef Drexel, 'The Relationship between the Legal Exclusivity and Economic Market Power' in Inge Govaere and Hanns Ullrich (eds.), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, pp.22-23.

<sup>181</sup> Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexel (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, fn 81.

<sup>182</sup> *ibid*, pp.70-71.

<sup>183</sup> *ibid*, pp.72-73. Similar opinion has been expressed also in Thomas Eilmansberger, 'How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses' (2005) 42 *Common Market Law Review* 129, p160. Thomas Eilmansberger, 'The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after IMS Health and Microsoft?' (2005) 16 *King's College Law Journal* 329, p336.

<sup>184</sup> Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexel (ed.), *Research handbook on intellectual property and competition law* (Edward Elgar, 2008) 54, p76.

particularly in the markets where competition is vulnerable owing to the network effect or interoperability requirement as in *Microsoft*.<sup>185</sup> Thus, contestable-market theory requires a much greater space for contestability in these conglomerate markets.<sup>186</sup>

### 3.2 Business performance justification

From the perspective of applicable justifications, Eilmansberger suggests a *business performance justification* approach, which explores the causal relation between business efforts and the creation of the essential input.<sup>187</sup> According to Eilmansberger, refusal to grant access to essential IPR could be justified on the ground that the input concerned represents “an effort to compete on merits”.<sup>188</sup> Specifically, this justification could be successfully invoked only if the business investment on the input intentionally aims at a specific downstream market.<sup>189</sup> Accordingly, this justification would be denied in following situations: (1) the input is primarily designed for another downstream market which is not involved in the specific case; (2) the input does not represent the result of superior business effort, but is merely the side-product of the development and manufacture of another product, i.e. interface information (*Microsoft*), or copyrighted forms or appearances (*Volvo*); (3) the input is certain information regarding the primary product, the production of which is not particularly onerous or requires additional innovative efforts, i.e. user guides or TV program listing (*Magill*); (4) the input has been transferred from the State to the present holder after the course of privatization, i.e. telecommunications networks.<sup>190</sup> In most preceding EU cases the accused undertakings were not eligible to invoke this *business performance justification* for a refusal to license since their IPRs were either the by-products of the primary products, or did not require particular superior business efforts. The only appropriate case might be *IMS Health*.<sup>191</sup> The creation of the ‘1860 brick structure’ was directed at serving the downstream market (or the subsequent production stage), and its development required significant business efforts. However, the participation of its potential customers contributed to the creation of the brick structure and it reduces the

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<sup>185</sup> Ibid.

<sup>186</sup> Ibid.

<sup>187</sup> Thomas Eilmansberger, ‘How to distinguish good from bad competition under article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses’ (2005) 42 *Common Market Law Review* 129, pp.165-166.

<sup>188</sup> *ibid*, p165.

<sup>189</sup> *ibid*, p165.

<sup>190</sup> *ibid*, pp.165-166. For the fourth point, see also John Temple Lang, ‘The Principle of Essential Facilities in European Community Competition Law – the Position since Bronner’ (2000) 1 *Journal of Network Industries* 375, pp.375-376.

<sup>191</sup> Thomas Eilmansberger, ‘The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after *IMS Health* and *Microsoft*?’ (2005) 16 *King’s College Law Journal* 329, p345.

persuasiveness of the *business performance justification* in that case.

### 3.3 Open-ended approach

As mentioned before, the Commission in its *Microsoft* decision denied the “existence of an exhaustive checklist of exceptional circumstances” when evaluating the potentially abusive refusal, and maintained that it would base its decision on a comprehensive examination of the entire circumstances of a specific refusal case.<sup>192</sup> Such an open-ended approach has been criticized because it risks transforming the possibility of finding an abusive refusal to license from the exception into the rule.<sup>193</sup> Nevertheless, such an approach is contended to have been inferred, to some extent, in the General Court’s judgment in *Microsoft* and the wording of Article 102(b) TFEU, both of which imply that other types of exceptional circumstances could also fall within the ‘exceptional circumstances test’.<sup>194</sup> Therefore, this open-ended approach addresses the concern at the intersection of competition law and intellectual property rights, as the Commission concluded, by evaluating the entire circumstances of a specific case and balancing the anti-competitive effects on the relevant market against its pro-competitive effects on a case-by-case basis. In general, this approach will take into consideration of circumstantial factors *inter alia* market power, network effects, monopoly leveraging, predatory intent, and the degree of follow-on innovation, to examine whether the competition *in* the market (i.e. price competition) or competition *for* the market (i.e. innovation competition) has been suppressed by means of eliminating existing competitors or impeding the entry of potential competitors.<sup>195</sup> Besides, the specific subject matter protected and the economic rationale of the exclusive right conferred may also affect the assessment.<sup>196</sup> If a *prima facie* abuse has been established, this approach will consider whether the proposed pro-competitive factors could outweigh the negative effects. In the case that the refusal at stake is alleged to preserve incentive to innovate, as analyzed before, the causal connection between IP protection and incentive to innovate shall be investigated.<sup>197</sup>

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<sup>192</sup> Case COMP/C-3/37.792 *Microsoft* Decision, Para 555 and 558.

<sup>193</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p103.

<sup>194</sup> Steven Anderman, ‘Does the Microsoft case offer a New Paradigm for the “exceptional circumstances” test and compulsory copyright licenses under EC competition law?’, (2004) 1(2) *The Competition law review* 7, p13.

<sup>195</sup> Kelvin Hiu Fai Kwok, ‘A New Approach to Resolving Refusal to License Intellectual Property Rights Disputes’, (2011) 34(2) *World Competition* 261, pp.273-283.

<sup>196</sup> Josef Drexler, ‘The Relationship between the Legal Exclusivity and Economic Market Power’ in Inge Govaere and Hanns Ullrich (eds), *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 13, p32.

<sup>197</sup> See *supra* subsection 2.5.1 Refusal to license vs. refusal to supply. See also Kelvin Hiu Fai Kwok, ‘A New Approach to Resolving Refusal to License Intellectual Property Rights Disputes’, (2011) 34(2) *World Competition* 261, pp.283-286.

As analyzed in the foregoing paragraph, open-ended approach weighs the net effect of the refusal concerned in a more economic way. The competition authorities should order a compulsory licensing only if such intervention brings about an increase in overall welfare, namely when the following equation is satisfied:<sup>198</sup>

$$\Delta W_1 + \Delta W_2 > 0,$$

In above equation,  $\Delta W_1$  and  $\Delta W_2$  respectively represent the variation in welfare brought about by the compulsory license for current period and for the future. The immediate welfare variation  $\Delta W_1$  is calculated as follows:

$$\Delta W_1 = \Delta(Tv_1 - Tc) - Ca$$

$Tv_1$  is the total value gained by consumers in this period;  $Tc$  and  $Ca$  are proxies for the total cost and the authority's administrative cost in its decision making. The variation in total cost for current period involves the cost variation on the part of the dominant undertaking and that of new entrants:

$$\Delta Tc = \Delta Cd + \Delta Cc$$

$\Delta Cd$  in above equation represents the increased cost of the dominant undertaking incurred by the compulsory licensing, and  $\Delta Cc$  is the reduction in cost for the competitors who otherwise have to depend on other possible substitutes that are not so effective and efficient. The calculation of the welfare variation in the future period  $\Delta W_2$  involves the estimated change in total value to be brought by expected innovation on the part of the dominant undertaking or its competitors, and total cost the variation on which however could almost be ignored.<sup>199</sup>

$$\Delta W_2 = \Delta E (Tv_2 - Tc).$$

However, according to Larouche, most of these values and costs in the equations, particularly  $\Delta Cd$  and  $\Delta Tv_2$ , are difficult to quantify in a specific refusal case where available information is insufficient to process the prediction.<sup>200</sup> Therefore, the design of the four prongs of the 'exceptional circumstances test' is to provide workable proxies to assess the overall welfare: (1) the requirement of indispensability aims to guarantee the reduction in cost for the competitors  $\Delta Cc$  is high; otherwise, if the cost of other possible alternatives is low without the intervention,  $\Delta Tv_1$  will be limited; (2) the condition of elimination of effective competition and the new product condition are designed to firstly indicate that  $\Delta Tv_1$  is positive, and their second

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<sup>198</sup> Following analysis and economic equations are basically based on Pierre Larouche's article, 'The European Microsoft Case at the Crossroads of Competition Policy and Innovation: Comment on Ahlborn and Evans' (2009) 75 *Antitrust Law Journal* 933, pp.948-952.

<sup>199</sup> *ibid*, fn 80, p949.

<sup>200</sup> *ibid*, p949.

function is to examine  $\Delta W_2$  by predicting whether the dominant undertaking's incentive to innovate will be negatively affected to a significant degree by the introduction of a new product from its competitor; (3) the justification, if relating to incentive to innovate, is an indicator of  $\Delta W_2$ .<sup>201</sup> It appears that these proxies do not constitute an exhaustive list of exceptional circumstances since only a few elements, such as  $\Delta Cc$ ,  $\Delta Tv_1$  and  $\Delta W_2$ , have been included. Therefore, it is not appropriate to exclude the possibility that there could be other applicable proxies (i.e. a disruption of previous levels of disclosure, existence of a super-dominant position on the neighbouring market) which could contribute to approximating the first equation above and thus improve the quality of the assessment.<sup>202</sup>

#### 4. Preliminary conclusion

Prior to the *Microsoft I* case, the 'exceptional circumstances test' was designed to carefully delineate "the occasions when the owner of IPRs enjoying a real economic monopoly can be charged with abuse by judicial authority", leaving "extensive scope for the legitimate exercise of IPRs by their owner".<sup>203</sup> The mere achievement of a dominant position on the relevant market and the possession of essential intellectual property rights apparently would not be considered as abuse under competition rules since it results from both the IPR owner's investments on the innovation activities and intense competition in the market that selects the superior and eliminates the inferior. The Article 102 TFEU would not intervene the autonomy of a dominant undertaking and compel it to enter into a license contract with another undertaking, unless the IPR as an input is indispensable for the appearance of a new product on the downstream market with unmet consumer demand and such a refusal would lead to elimination of all the competition in the downstream market. Against the background of modernization of Article 102 TFEU, the result of EU *Microsoft I* case demonstrates that the EU Commission and EU Courts (at least the General Court) have adopted a loose interpretation of the 'exceptional circumstances test', *inter alia* on the requirement of the appearance of a new product, thus display EU's interventionist stance in the high-tech industries where exist strong network effects. This stance is more obvious in the absence of a practical guidance on the justification prong that enables the accused undertaking to defend his enforcement of intellectual property right. The next section will turn to investigate the position held on the other side of the Atlantic Ocean on refusal to license. Although one of the remedies in the US

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<sup>201</sup> *ibid*, pp.949-950.

<sup>202</sup> *ibid*, pp.950-951.

<sup>203</sup> Steven Anderman, 'Does the Microsoft case offer a New Paradigm for the "exceptional circumstances" test and compulsory copyright licenses under EC competition law?', (2004) 1(2) *The Competition law review* 7, p9.

*Microsoft* case similarly required Microsoft to disclose certain communications protocol to interested parties on FRAND terms,<sup>204</sup> the main abusive conduct accused by the Department of Justice is unlawful tying Microsoft's web browser with its Windows operating system. Thus due to the limited subject of this research, the abusive conduct and its consequent effects on the competition process and consumer welfare in the US *Microsoft* case will not be compared with the refusal to license part – but not the tying part – of the EU *Microsoft I* case.

## 5. The US approach

### 5.1 Intersection of antitrust and IPR in the US: certainties and uncertainties

At the intersection of antitrust rules and IPR protection, the competition authority and courts on the other side of the Atlantic Ocean similarly starts from the general principle – since nearly 100 years before – that every undertaking, holding a dominant position or not, is free to choose its trading partner and this economic freedom should generally not be restricted by the antitrust rules.<sup>205</sup> As mentioned before, on the relationship between IPR and market dominance, EU competition authorities have stated in many occasions that the mere possession of IPR does not demonstrate the existence of a dominant position.<sup>206</sup> An IPR grants the holder exclusive rights to prevent others from copying, producing, marketing or importing certain products protected by such IPR without the owner's consent. However, such exclusiveness does not lead to the monopoly in the competition context. In the relevant market there may be interchangeable products, which exert competitive constraints on the IPR holder. This has also been accepted by the US Supreme Court.<sup>207</sup> Neither of the Appellate Courts in *Kodak*<sup>208</sup> or in *Xerox*<sup>209</sup> presumed that the OEMs had market power due to their patents.

With regard to the exercise of IPR particularly, first of all, the US Supreme Court in the case *Continental Paper Bag v. Eastern Paper Bag*<sup>210</sup> established that generally the IPR holder has no duty to use his exclusive right, stating that “such exclusion may be said to have been of the very essence of the right conferred by the patent, as it is the privilege of any owner of property

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<sup>204</sup> Final Judgment, *US v. Microsoft*, Civil Action No. 98-1232 (CKK), entered November 12, 2002, Para III E.

<sup>205</sup> See e.g. *Verizon Communications Inc. v. Law Office of Curtis V. Trinko* (hereinafter ‘*Trinko*’), 540 U.S. 398 (2004).

<sup>206</sup> See chapter 2, footnote 210.

<sup>207</sup> *Illinois Tool Works Inc. et al. v. Independent Ink, Inc.*, 547 U.S. 28 (2006), at 7.

<sup>208</sup> *Image Technical Services, Inc. v. Eastman Kodak Co.*, 125 F.3d 1195 (9<sup>th</sup> Cir. 1997), (hereinafter ‘*Kodak*’).

<sup>209</sup> *In re Independent Service Organizations Antitrust Litigation (CSU et al. v. Xerox Corporation)*, 203 F.3d 1322 (Fed. Cir. 2000), (hereinafter ‘*Xerox*’).

<sup>210</sup> *Continental Paper Bag v. Eastern Paper Bag*, 210 U.S. 405 (1908).



to use or not use it, without question of motive”.<sup>211</sup> On the freedom to refuse the IPR access request, Supreme Court and Courts of Appeals shared the same view on this issue in a number of cases prior to the *Kodak* and *Xerox* that mere exercising the IPR by refusing to license to third parties would not constitute an infringement under competition rules.<sup>212</sup> It is believed that, as held by the Court of Appeals for the First Circuit in *Data General Corporation v. Grumman System Support Corporation*, “while exclusionary conduct can include a monopolist’s unilateral refusal to license a copyright, an author’s desire to exclude others from use of its copyrighted work is a presumptively valid business justification for any immediate harm to consumers”.<sup>213</sup>

The fundamental US case law *Kodak* and *Xerox* both addressed this key issue at the interface of IPR and competition. However, neither has provided “sufficient guidance on potential antitrust liability for unilateral refusals to license”.<sup>214</sup> The divergent approaches adopted by the courts have generated “uncertainty for licensors and licensees”.<sup>215</sup> In both cases the basic facts were similar that Independent Service Organizations (ISOs) alleged that the Original Equipment Manufacturers (OEMs) had infringed antitrust rules by refusing to supply patented parts. In *Kodak* the Ninth Circuit held that OEMs’ refusals to license patented or copyrighted products were “presumptively legitimate”, but on the other hand the “presumption may also be rebutted by evidence of pretext.”<sup>216</sup> Such an *evidence of pretext* was found in *Kodak* because the defendant refused to sell both patented and unpatented parts and was not even conscious of its rights when it did so.<sup>217</sup> It thus could be concluded that whether the refusal to license in question constitutes infringement depends on the *intent* of the IPR holder. In contrast with *Kodak*’s uncertainty, in *Xerox* the court adopted a quasi-immunity approach for intellectual property right. The “patentee’s subjective motivation for refusing to sell or license its patented

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<sup>211</sup> *ibid*, p429.

<sup>212</sup> See e.g. *Hartford-Empire Co. v. United States*, 323 U.S. 386 (1945); *Miller Insituform, Inc. v. Insituform of N. Am., Inc.*, 830 F.2d 606 (6th Cir. 1987); *United States v. Westinghouse Elec. Corp.*, 648 F.2d 642 (9th Cir. 1981); *SCM Corp. v. Xerox Corp.*, 645 F.2d 1195 (2d Cir. 1981); *Simpson v. Union Oil Co. of Cal.*, 377 U.S. 13 (1964).

<sup>213</sup> *Data General Corporation v. Grumman System Support Corporation*, 36 F.3d 1147, 1187 (1<sup>st</sup> Cir. 1994).

<sup>214</sup> U.S. Department of Justice and Federal Trade Commission, ‘Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition’, (2007), p 16. Available at <http://www.ftc.gov/sites/default/files/documents/reports/antitrust-enforcement-and-intellectual-property-rights-promoting-innovation-and-competition-report.s.department-justice-and-federal-trade-commission/p040101promotinginnovationandcompetitionrpt0704.pdf>, last visited on 20 July 2014.

<sup>215</sup> *ibid*.

<sup>216</sup> *Kodak*, 125 F.3d 1195, 1219.

<sup>217</sup> *ibid*, 1219-1220.

products” was not in the court’s consideration.<sup>218</sup> The rebuttable presumption in *Kodak* case was replaced by a quasi *per se* legal presumption with only three exceptions: “illegal tying, fraud in the Patent and Trademark Office, or sham litigation.”<sup>219</sup>

It is claimed that *Kodak* approach is better because it is capable of distinguishing anti-competitive conducts from pro-competitive ones and striking a balance between the IPR holder’s interest and the public interest.<sup>220</sup> However, the intent-based approach has been generally criticised since it is nearly impossible to operate in practise.<sup>221</sup> According to *Kodak* approach, a refusal motivated by a desire to exercise its IPR and protect its investment is permitted and a refusal motivated by a desire to strengthen its monopoly power or to leverage such power into neighbouring market is prohibited. The *intent*, however, is very difficult to detect and to prove. It would create the risk of wrongly prohibiting pro-competitive conducts or permitting anti-competitive conducts. Thus the incentives of the IPR holders to investment and to research would be chilled since legitimacy of their behaviour may not be estimated and guaranteed beforehand. Therefore, the focus should be “upon the effect of [the] conduct, not upon the intent behind it”.<sup>222</sup> The role of the IPR holder’s intent is to “help to interpret facts and to predict consequences”<sup>223</sup> but not to decide the case. On the other hand, antitrust immunity for refusal to license adopted in *Xerox* has also been criticised, as in general such a broad immunity approach would mistakenly protect anti-competitive refusals which are to the detriment of consumers.<sup>224</sup> The so called *three exceptions* – illegal tying, fraud in the Patent and Trademark Office, or sham litigation – actually concern the validity of IPR or other abusive practice but have no relevance with the assessment on the substance of the refusal at issue. Furthermore, such general immunity is inconsistent with the more economic approach - currently prevailing both in the EU and US – which takes all relevant, surrounding circumstances into consideration and analyzes on a case-by-case basis.<sup>225</sup> The divergent approaches between *Kodak* and *Xerox* have triggered an intense debate on whether a categorical exemption from antitrust liability for unilateral, unconditional refusal to license

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<sup>218</sup> *Xerox*, 203 F.3d 1322, 1327.

<sup>219</sup> *ibid.*

<sup>220</sup> U.S. Department of Justice and Federal Trade Commission, ‘Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition’, (2007), *supra* note 215, p17.

<sup>221</sup> *ibid.*

<sup>222</sup> *United States v Microsoft Corp.*, 253 F.3d 34, 59 (D.C. Cir. 2001).

<sup>223</sup> *Chicago Board of Trade v. United States* 246 U.S. 231, 238 (1918).

<sup>224</sup> U.S. Department of Justice and Federal Trade Commission, “Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition”, (2007), *supra* note 215, pp.18-19.

<sup>225</sup> *ibid.*, p19.

should be favoured, or antitrust intervention should be allowed under narrow circumstances.<sup>226</sup> While the viewpoints among the antitrust practitioners and policymakers still differ widely, US antitrust authorities conclude that *pure* refusal to license will generally not attract antitrust intervention by stating that “liability for mere unconditional, unilateral refusals to license will not play a meaningful part in the interface between patent rights and antitrust protection...there are numerous imaginable scenarios that involve conduct that goes beyond a mere refusal to license a patent and could give rise to antitrust liability.”<sup>227</sup>

## 5.2 Who protects consumer, who protects competitor?

In general, while EU competition authorities are more willing to intervene and to stress the necessity of short-term competition, “which may result in a certain over-deterrence”, US antitrust authorities appear to be reluctant to step in and “expect the market will correct itself”<sup>228</sup> on the ground that the courts are not supposed “to act as central planners, identifying the proper price, quantity, and other terms of dealing” and they should not “to assume the day-to-day controls characteristic of a regulatory agency”<sup>229</sup>. Such divergent attitudes may originally stem from the different philosophies of two jurisdictions, which could be reflected, during their application in relevant laws, by the distinct proportions of attention which have been paid by the EU and US’s competition authorities on balancing some social and economic values, such as efficiency and social equity, consumer welfare and rivalry preservation.<sup>230</sup> The US antitrust law focuses more on efficiency.<sup>231</sup> The US antitrust authorities are lenient on unilateral commercial behaviour conducted by dominant undertakings and see less danger

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<sup>226</sup> See e.g. Hearing on Competition and Intellectual Property Law and Policy in the Knowledge Based Economy Strategic Use of Licensing: Is There Cause for Concern about Unilateral Refusals to Deal?, co-hosted by Department of Justice Antitrust Division and Federal Trade Commission, Washington, D.C., 1 May 2002. Available at <http://www.ftc.gov/opp/intellect/020501xscript.pdf>, last visited on 22 Dec 2011. See also e.g. Herbert J. Hovenkamp, Mark D. Janis and Mark A. Lemley, ‘Unilateral Refusals to License in the U.S.’ (2006) 2 *Journal of Competition Law & Economics* 1; Mark R. Patterson, ‘When is Property Intellectual? The Leveraging Problem’, (2000) 73 *Southern Californian Law Review* 1133; Sharon Brawner McCullen, ‘The Federal Circuit and Ninth Circuit Face-off: Does a Patent Holder Violate the Sherman Act by Unilaterally Excluding Others from a Patented Invention in More than One Relevant Market?’, (2001) 74 *Temple Law Review* 469; R Hewitt Pate, ‘Refusals to Deal and Intellectual Property Rights’, (2002) 10 *George Mason Law Review* 429.

<sup>227</sup> U.S. Department of Justice and Federal Trade Commission, “Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition”, (2007), *supra* note 215, p32.

<sup>228</sup> Hans Henrik Lidgard, ‘Application of Article 82 EC to Abusive Exclusionary Conduct – Refusal to Supply or to License’, (2009) 4 *Europarättslig tidskrift*, 694, p701.

<sup>229</sup> *Trinko*, 540 U.S. 398, 408 and 415.

<sup>230</sup> Mark Furse, ‘Competition Law Choice in China’, (2007) 30(2) *World Competition* 323, pp.325-326.

<sup>231</sup> See Katarzyna A. Czapracka, ‘Where Antitrust Ends and IP Begins-On the Roots of the Transatlantic Clashes’, (2007) 9 *Yale Journal of Law & Technology* 44, pp.55-57.

towards competition from such business tactics. They “see little scope for antitrust policy to mitigate the consequences of imperfect IP policies”<sup>232</sup>, based on the belief that “any competitive concerns are better remedied by changes in the IP policy.”<sup>233</sup> The EU competition authority, however, is more aggressive to ensure that the trade between Member States is not adversely affected by the unilateral conducts of dominant undertakings. EU Competition authorities “perceive [the] competition process as vulnerable and are more eager to address perceived distortions”<sup>234</sup>, since they “see a role for competition law to correct improvidently defined IPRs, even if it entails adjusting competition principles.”<sup>235</sup> It is also worth noting that against the background of lack of harmonized patent/copyright law at the EU level, EU Commission has confronted a further complicated situation at the interface between competition rules and IPR protection than its US counterparts.<sup>236</sup>

The different manners of the EU and US competition authorities towards dominant undertakings’ commercial freedom also impact the balancing of competitor interest and the consumer welfare in refusal cases. Although EU Commission claims that it only concerns consumer welfare but not the protection of competitors,<sup>237</sup> it has been contended that the EU competition authority has “focused on preserving rivalry rather than on efficiency”.<sup>238</sup> One negative trend of such over-protection may be that some disadvantaged competitors, in order to win back the market position, try to rely on judicial limitation imposed on the dominant undertaking rather than to compete on the merits. The former US officer in charge of

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<sup>232</sup> *ibid*, abstract.

<sup>233</sup> *ibid*, p100.

<sup>234</sup> *ibid*, p57.

<sup>235</sup> *ibid*, abstract.

<sup>236</sup> Heike Schweitzer, ‘Controlling the Unilateral Exercise of Intellectual Property Rights: A Multitude of Approaches but No Way Ahead?’ in Inge Govaere and Hanns Ullrich (eds.) *Intellectual Property, Market Power and the Public Interest* (P.I.E. Peter Lang, 2008) 59, p71.

<sup>237</sup> See e.g. Speech of Director-General for Competition Alexander Italianer, ‘Prepared remarks on: Level-playing field and innovation in technology markets’, at Conference on Antitrust in Technology, Palo Alto (US), 28 Jan 2013, available at [http://ec.europa.eu/competition/speeches/text/sp2013\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2013_01_en.pdf), last visited on 20 July 2014, p6: “Like in the US, the aim of the Commission’s enforcement activity in relation to exclusionary conduct is to ensure that dominant undertakings do not impair effective competition by foreclosing their competitors in an anticompetitive way. We are not concerned about protecting competitors as such. We are only concerned about ‘anticompetitive foreclosure’ that is likely to lead to an adverse impact on consumer welfare, in the form of higher prices or by limiting quality, innovation and consumer choice.”

<sup>238</sup> Rick Rule, Steve Houck, Doug Melamed and Joe Watershed, ‘The EC Decision against Microsoft: Windows on the World, Glass Houses, or Through the Looking Glass’, *The Antitrust Source*, (September 2004), available at [http://www.americanbar.org/content/dam/aba/publishing/antitrust\\_source/Sep04MSBB.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Sep04MSBB.authcheckdam.pdf), last visited on 20 Dec 2012, p19.

Department of Justice's Antitrust Division issued the following statement after the General Court's judgment in *Microsoft*:

"We are, however, concerned that the standard applied to unilateral conduct by the [General Court], rather than helping consumers, may have the unfortunate consequence of harming consumers by chilling innovation and discouraging competition. In the United States, the antitrust laws are enforced to protect consumers by protecting competition, not competitors. In the absence of demonstrable consumer harm, all companies, including dominant firms, are encouraged to compete vigorously. U.S. courts recognize the potential benefits to consumers when a company, including a dominant company, makes unilateral business decisions, for example to add features to its popular products or license its intellectual property to rivals or to refuse to do so."<sup>239</sup>

However, protecting competitors is one path to reach the ultimate goal of consumer welfare, which has been in the heart place of EU competition policy. According to the Commission Guidance, the existence of competitive constrain from rivalry is necessary to ensure that the efficiency brought about by the dominant undertaking would be passed onto the consumer.<sup>240</sup> From this perspective, it makes some sense to protect competitors from exclusionary practices. On the other hand, it is claimed that the EU Commission and EU Courts have worried too much about the actual existence of a sufficient number of competitors and has erroneously related the promotion of consumer welfare to the preservation of a certain amount of competitors.<sup>241</sup> This may be the reason why in fast-moving industries, where 'winner takes all' due to first mover advantage, the EU competition authority appears to lack confidence than its counterparts on the other side of the Atlantic Ocean, which finally leads to the EU Commission's tougher remedy imposed on Microsoft.<sup>242</sup>

## 6. Conclusion

The Court of Justice in *Magill* established the main principle in refusal to license IPR cases that "the exercise of an exclusive right by the proprietor may, in exceptional circumstances, involve

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<sup>239</sup> Press release by Thomas O. Barnett, Assistant Attorney General for the Department's Antitrust Division, on European Microsoft Decision, Washington, 17 September 2007, available at [http://www.justice.gov/atr/public/press\\_releases/2007/226070.htm](http://www.justice.gov/atr/public/press_releases/2007/226070.htm), last visited on 23 Dec 2011.

<sup>240</sup> See Commission Guidance, *supra* note 65, Para 30.

<sup>241</sup> Roberto Pardolessi and Andrea Renda, 'The European Commission's Case Against Microsoft: Kill Bill?', (2004) 27(4) *World Competition* 513, p565.

<sup>242</sup> *ibid*, p566.

abusive conduct”.<sup>243</sup> The EU Commission and Courts however have been at pains in the following cases, including *Magill*, *IMS Health* and *Microsoft I*, to interpret the content of the ‘exceptional circumstances test’, namely the three prongs of exceptional circumstances and one prong of justification, in order to improve the legal certainty of the assessment framework for the competition authorities and courts at Member States’ level and the competition law practitioners. EU *Microsoft I* case, as a milestone exclusionary case under the framework of Article 102 TFEU, has provided the EU Commission and General Court a good opportunity to re-consider the application of the ‘exceptional circumstances test’ in the fast-moving industries and more detailed meaning of each condition. After having adopted lower criteria of the ‘exceptional circumstances test’ *inter alia* the stricter new product requirement has been broadened to include technical development brought about by follow-on innovations in the relevant market, the EU Commission has demonstrated its interventionist stance towards the refusal behaviour by an undertaking with monopoly market power in a market characterized by strong network effects. This stance is even more obvious when compared to the US antitrust authorities’ generally lenient approach on unconditional, unilateral refusal to license by a dominant undertaking. While the triumph in *Microsoft I* has encouraged the EU Commission to inquire the high-tech industries, it is not clear whether the tough remedy imposed on the software giant has impeded the incentives of other undertakings to innovate and invest, or the chilling effect is only psychological and negligible. The question of whether EU’s gradually weak *per se* lawful rule, or even “rule of reason analysis”<sup>244</sup> on refusal to license could be transposed to the Chinese legal and economic context, or the US lenient approach would fit better into the enforcement framework of China’s antitrust law will be analyzed in the next chapter.

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<sup>243</sup> Judgment in *Magill* ECLI:EU:C:1995:98, Para 50.

<sup>244</sup> Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p903.

## CHAPTER IV FRAND Related Issues

### 1. Refusal to license and the concept of FRAND

The term *fair, reasonable and non-discriminatory* ('FRAND') is a competition law-IPR intersection expression. Depending on whether the IP at issue is standard essential patent ('SEP') and whether the IPR holder has committed to standard-setting organizations ('SSOs') that he will license his IPR to third parties on FRAND terms, there might be two situations where the concept FRAND would be connected with the intellectual property rights owners' conduct of refusal to license. The concept FRAND emerges in non-SEP cases where the conduct of refusal to license IPR has, in exceptional circumstances, been considered abusive under Article 102 TFEU, irrespective of previous relationship between the licensor and the licensees. In those non-SEP cases, there might be two things an IPR holder who refuses to grant other undertakings a license to access to his IPR cares the most. One is, as analyzed in previous chapters, whether his refusal to license constitutes an abuse of dominant position under the competition rules. The other concern, as the subject of this chapter, is the follow-on pricing issue, namely how much benefits he could reap from licensing his IPR once his conduct of refusal to license has been considered as an abuse of dominant position. In EU Commission's decision in *IMS Health* case<sup>1</sup>, the Commission held that IMS should:

"license the 1860-brick structure on a non-discriminatory basis to NDC and AzyX. In any agreements in which IMS licenses the use of the 1860-brick structure, it is important to ensure that any fee which is charged is reasonable, and that the process does not take an undue amount of time, as this would frustrate the purpose of the order."<sup>2</sup>

Similarly in *Microsoft I* case<sup>3</sup>, the Commission required that:

"Microsoft Corporation shall [...] make the Interoperability Information available to any undertaking having an interest in developing and distributing work group server operating system products and shall, on reasonable and non-discriminatory terms, allow the use of the Interoperability Information by such undertakings for the purpose of developing and

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<sup>1</sup> Case COMP D3/38.044, NDC Health/IMS Health, Commission Decision, [2002] OJ L59/18 (3 July 2001), available in full at [http://ec.europa.eu/competition/antitrust/cases/dec\\_docs/38044/38044\\_15\\_5.pdf](http://ec.europa.eu/competition/antitrust/cases/dec_docs/38044/38044_15_5.pdf), last visited on 17 November 2013.

<sup>2</sup> Ibid, Para 215.

<sup>3</sup> Case COMP/C-3/37.792, Microsoft, Commission Decision, [2007] OJ L 32/23 (24 March 2004), available in full at [http://ec.europa.eu/competition/antitrust/cases/dec\\_docs/37792/37792\\_4177\\_1.pdf](http://ec.europa.eu/competition/antitrust/cases/dec_docs/37792/37792_4177_1.pdf), last visited on 17 November 2013.

distributing work group server operating system products”.<sup>4</sup>

Another situation could be the scenario where the SEP holder, who committed to license his SEP on FRAND terms<sup>5</sup>, seeks and enforces an injunction against specific third party before a court on the basis of his SEP. The EU Commission’s *Motorola Mobility* case<sup>6</sup> and *Samsung* case<sup>7</sup> belong to this category. Some Chinese firms have also been involved in FRAND commitment cases in the EU.<sup>8</sup> The main question in these cases is whether the seeking of a SEP-based injunction amounts to an abuse. Joaquín Almunia held that:

“Intellectual property rights are an important cornerstone of the single market. However, such rights should not be misused when they are essential to implement industry standards, which bring huge benefits to businesses and consumers alike. When companies have

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<sup>4</sup> Ibid, Article 5(a).

<sup>5</sup> For example, the IPR Policy of the European Telecommunications Standards Institute (‘ETSI’) provides that when an IPR holder discloses his essential IPR to the ETSI, the holder would be requested to give “an irrevocable undertaking in writing that it is prepared to grant irrevocable licences on fair, reasonable and non-discriminatory (‘FRAND’) terms and conditions” to those who seek such license and thus waive its right to refuse to grant a license. See ETSI IPR Policy, section 6.1, available at <http://www.etsi.org/images/files/IPR/etsi-ipr-policy.pdf>, last visited on 18 November 2013.

<sup>6</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, addressed to Motorola Mobility LLC relating to proceedings under Article 102 of the Treaty on the Functioning of the European Union and Article 54 of the EEA Agreement. Discussion of this case see the following section.

<sup>7</sup> Case COMP/C-3/39939 Samsung Electronics, Commission Decision of 29 April 2014 in accordance with Article 9 of Regulation 1/2003. In Samsung’s case, Samsung owns standard-essential patents for 3G UMTS standard, a key industry standard for mobile and wireless communications, and made a commitment to ETSI that it would license the patents which it had declared essential to the standard on FRAND terms. In 2011, Samsung started to seek injunctive relief before Member States’ courts against Apple based on claimed infringements of certain of its 3G UMTS standard-essential patents. The EU Commission on 29 April 2014 rendered commitments offered by Samsung legally binding under EU competition rules.

<sup>8</sup> Case C-170/13, Request for a preliminary ruling from the Landgericht Düsseldorf (Germany) lodged on 5 April 2013 — Huawei Technologies Co. Ltd v ZTE Corp., ZTE Deutschland GmbH, OJ C 215/5. The German court has stayed a current dispute between China’s largest telecommunications manufactures Huawei and ZTE on SEPs related to 4G/Long-Term-Evolution (‘LTE’) standard, and referred five questions to the CJEU seeking clarification on the compulsory license defence in SEP cases. On 11 September 2014 the Court of Justice heard the case. The Advocate General Wathelet on 20 November 2014 delivered opinion, in which the AG proposed an analytical framework to balance between the interests of SEP holder and the interests of any user of the technology. So far the Court of Justice has not delivered the judgment.

On top of the dispute with Huawei, ZTE is also involved in another FRAND commitment case. On 18 June 2014 ZTE Corp. filed an antitrust complaint with the EU Commission, requesting it to investigate whether Vringo Inc., a New York-based patent licensing company, has violated EU Competition rules by refusing to license its SEPs to ZTE on FRAND terms. See [http://www.zte.com.cn/en/press\\_center/news/201406/t20140619\\_425101.html](http://www.zte.com.cn/en/press_center/news/201406/t20140619_425101.html), last visited on 20 July 2014.



contributed their patents to an industry standard and have made a commitment to license the patents in return for fair remuneration, then the use of injunctions against willing licensees can be anti-competitive.”<sup>9</sup>

From the perspective of protection of innovation incentives, IPR holders should be compensated for their investment on R&D. From the perspective of competition policy, the prices that IPR holders ask for access to their IPRs should not be unduly high, since excessive pricing might trigger the competition authority’s investigation into whether such behaviour has again abused the IPR holder’s dominant market position assuming that “unfairly high pricing can be identified”.<sup>10</sup> Excessive pricing may raise competition concern not only in the EU<sup>11</sup>, but also in China<sup>12</sup>. In a recent Chinese anti-monopoly litigation between a Shenzhen-based telecom company Huawei Technology Co. (‘Huawei’) and US-based Inter Digital Co. (‘IDC’), Guangdong High Court upheld Shenzhen Intermediate Court’s finding that IDC had abused its dominant position by requiring Huawei to pay excessive royalties for its standard-essential patents for 3G wireless communication devices.<sup>13</sup> Therefore, for China it is also a crucial question under what conditions the IPR holders should license their IPRs, or specifically at what level the IPR holders should set the royalties once the conduct of refusal to license has been found unlawful. This chapter, firstly discusses the new set of ‘exceptional circumstances’ identified by the EU Commission in *Motorola* FRAND case, aiming to distinguish these conditions from the ‘exceptional circumstances’ recognized in non-SEP cases. Secondly, from a legal perspective, investigates EU and US’s approaches in

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<sup>9</sup> EU Commission press release, IP/12/1448, 21 December 2012, available at [http://europa.eu/rapid/press-release\\_IP-12-1448\\_en.htm](http://europa.eu/rapid/press-release_IP-12-1448_en.htm), last visited on 17 November 2013.

<sup>10</sup> Eleanor M. Fox, ‘Monopolization and Dominance in the United States and the European Community: Efficiency, Opportunity, and Fairness’ (1986) 61 *Notre Dame Law Review* 981, p992.

<sup>11</sup> For example, Vice President of the EU Commission Joaquín Almunia stressed once again that excessive pricing is covered by Article 102 TFEU, in his speech *Competition in the Online World*, delivered on 11 November 2013, London, available at [http://europa.eu/rapid/press-release\\_SPEECH-13-905\\_en.htm](http://europa.eu/rapid/press-release_SPEECH-13-905_en.htm), last visited on 18 November 2013.

<sup>12</sup> *Anti-Monopoly Law of the People's Republic of China* (Adopted at the 29th meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China on 30 August 2007, translation available by [subscription](http://www.lawinfochina.com/display.aspx?id=6351&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%C2%A2%B6%CF%B7%A8) at <http://www.lawinfochina.com/display.aspx?id=6351&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%C2%A2%B6%CF%B7%A8>, last visited on 29 October 2013, hereinafter ‘AML’), Article 17(1).

<sup>13</sup> The first instance decision of Shenzhen Intermediate Court has not been published due to business secrets reason. The final judgment of Guangdong High Court has been publicly available at <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20140417030902158689>, last visited on 20 July 2014. However, the royalty rate-related information in the judgment is not accessible due to business secrets reason. The analysis of this case could see *infra* chapter 5, section 5.2.2.

determining a FRAND royalty rate. Thirdly, this chapter from an economic perspective introduces some approaches to determining a FRAND royalty rate. Then, this chapter analyzes their applicability in the follow-on refusal to license cases.

## **2. New set of ‘exceptional circumstances’ in EU Commission’s *Motorola* FRAND case**

In *Motorola* FRAND case, Motorola Mobility holds standard-essential patents for GPRS standard, which is also a key industry standard for mobile and wireless communications, and gave a commitment to ETSI that it would license the patents which it had declared essential to the standard on FRAND terms to requesting parties. Motorola Mobility sought an injunction against Apple in Germany based on claimed infringement of certain of its GPRS standard-essential patents. The EU Commission adopted a decision on 29 April 2014 finding that Motorola Mobility’s seeking a SEP-based injunction constitutes an abuse of a dominant position prohibited by EU competition rules.<sup>14</sup> As to the balance between the exercise of intellectual property rights and the protection of market competition, the Commission reiterated the general principle, as well acknowledged in previous case law,<sup>15</sup> that the right owner, including a holder of SEPs, has the right to exercise its rights by seeking and enforcing injunctions before courts, or to license its rights and obtain remuneration.<sup>16</sup> The exercise of intellectual property rights will be treated as abuse of dominant position only in exceptional circumstances and if there is no any objective justification.<sup>17</sup>

Since the list of abusive practices provided by Article 102 TFEU is not exhaustive but merely examples of abuse of a dominant position,<sup>18</sup> the Commission maintained that it is necessary to take all relevant circumstances into account to determine whether an undertaking has

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<sup>14</sup> Case AT.39985 – *Motorola*, Commission Decision of 29 April 2014, addressed to Motorola Mobility LLC relating to proceedings under Article 102 of the Treaty on the Functioning of the European Union and Article 54 of the EEA Agreement.

<sup>15</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, Para 7-8; Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para. 49; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para. 34 Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 331.

<sup>16</sup> Case AT.39985 – *Motorola*, Commission Decision of 29 April 2014, para 278 and 282.

<sup>17</sup> *Ibid*, para 278.

<sup>18</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, para 9; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, para 36-38; Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI:EU:T:2007:289, para 860; Judgment in *Deutsche Telekom v Commission*, C-280/08 P, ECLI:EU:C:2010:603, para 173; and Judgment in *TeliaSonera*, C-52/09, ECLI:EU:C:2011:83, para 26.

abused a dominant position.<sup>19</sup> Thus, in exceptional circumstances restrictions on a dominant undertaking's right to enforce its IP by seeking to obtain an injunction from a court may be ordered. Such exceptional circumstances could be found in non-SEP scenario, such as the *IMS Health* case, but also in the SEP scenario like this *Motorola* case.<sup>20</sup>

In *Motorola* FRAND case, the Commission considered that, by committing to license on FRAND terms, Motorola “has chosen to monetise its standard essential technology through licensing on fair, reasonable and non-discriminatory terms and not to use it to exclude implementers of the GPRS standard provided that it is appropriately remunerated for the use of its technology.”<sup>21</sup> In other words, according to the Commission, Motorola made a binding commitment to allow other standard implementers to make use the SEPs in exchange for a reasonably set licensing fee, but not to exercise its SEPs in a manner that will exclude others from the market.<sup>22</sup> The EU Commission found that the standardisation context and Motorola's FRAND commitment constitute ‘exceptional circumstances’, thus distinguishing this case from other cases where the general principle that a patent holder has the right to refuse to license could apply.<sup>23</sup> What's more, due to the fact that this is the first case where the Commission delivers its opinion on SEP-related issue in the form of an infringement decision, the Commission left much space for the future cases by maintaining that Motorola's seeking and enforcement of an SEP-based injunction may serve as one example that give rise to liability under Article 102 TFEU.<sup>24</sup> The Commission held that in other SEP-related cases whether there is an abuse of dominant position must be examined according to specific circumstances of each case and it cannot be inferred from this *Motorola* decision.<sup>25</sup>

According to the Commission, Motorola's behaviour of seeking and enforcement of an SEP-based injunction resulted in not only a temporary ban on the online sale of Apple's GPRS-compatible products in Germany, but also the inclusion in the Settlement Agreement of licensing terms disadvantageous to Apple.<sup>26</sup> The latter anti-competitive effect – inclusion disadvantageous licensing terms in the Settlement Agreement – includes, *inter alia*, the

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<sup>19</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 532.

<sup>20</sup> Ibid, para 531-533.

<sup>21</sup> Ibid, para 294.

<sup>22</sup> Ibid, para 299.

<sup>23</sup> Ibid, para 281-300.

<sup>24</sup> Ibid, para 534.

<sup>25</sup> Ibid.

<sup>26</sup> Ibid, section 8.2.3.1 and 8.2.3.2. Apart from these effects on Apple, according to the Commission, Motorola's behaviour was also capable of having a negative impact on standard-setting, see section 8.2.3.3.

termination clause by which Motorola is entitled to terminate the license once Apple challenges the validity of the patents concerned,<sup>27</sup> and Apple's acceptance of which was not driven by normal bargaining considerations but by Motorola's abusive behaviour.<sup>28</sup> Apparently, by the anti-competitive effects brought about by Motorola's seeking and enforcement of an SEP-based injunction, the abusive practice in this case could be clearly distinguished from the unconditional refusal to license behaviour (the main subject of this research), the main purpose of which is to exclude competitors from the market. In this case, it seems Motorola's refusal to license behaviour is merely a means in negotiation to threaten the standard implementers to conclude the licensing agreements in favour of the SEP holder.

Concerning the objective justification, the Commission reiterated that the mere possession of IP rights cannot constitute an objective justification for the right holder's seeking and enforcement of an injunction against a potentially willing licensee.<sup>29</sup> The EU competition law allows an undertaking in a dominant position to take reasonable steps as it deems appropriate to protect its commercial interests.<sup>30</sup> According to the Commission, a SEP holder is entitled to protect its interests by seeking and enforcing an injunction, for instance, in the following circumstances:

- “(a) the potential licensee is in financial distress and unable to pay its debts;
- (b) the potential licensee's assets are located in jurisdictions that do not provide for adequate means of enforcement of damages; or
- (c) the potential licensee is unwilling to enter into a licence agreement on FRAND terms and conditions, with the result that the SEP holder will not be appropriately remunerated for the use of its SEPs. The corollary of a patent holder committing, in the standardisation context, to license its SEPs on FRAND terms and conditions is that a potential licensee should not be unwilling to enter into a licensing agreement on FRAND terms and conditions for the SEPs in question.”<sup>31</sup>

The analysis of the Commission in its decision demonstrates that Apple's second Orange Book offer<sup>32</sup> clearly indicated that Apple was not unwilling to enter into a licence agreement

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<sup>27</sup> Ibid, section 8.2.3.2.1.1.

<sup>28</sup> Ibid, para 412.

<sup>29</sup> Ibid, para 423.

<sup>30</sup> Judgment in *United Brands*, 27/76, ECLI:EU:C:1978:22, para 189.

<sup>31</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 427.

<sup>32</sup> See as summarized in Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 125 and 126. The Orange Book judgment was issued by the German Federal Court on 6 May 2009 (case no. KZR 39/06), concerning a patent infringement and injunction claim based on a non-SEP against an implementer of patented CD-Rs and

on FRAND terms and conditions with Motorola.<sup>33</sup> With regard to the efficiency defense, the Commission maintained that the alleged advantages put forward by Motorola in terms of efficiency could not counteract the likely anti-competitive effects, thus not capable of justifying its behaviour of seeking and enforcement of an SEP-based injunction against Apple.<sup>34</sup>

Moreover, the Commission rejected Motorola's argument that its seeking and enforcing an injunction was in line with the requirements of the Orange Book judgment.<sup>35</sup> The Commission explained that, first, the German courts' decision could not eliminate Motorola's responsibility under Article 102 TFEU since "Motorola had full discretion throughout the German proceedings to decide whether to seek an injunction in the first place and whether to enforce the injunction once it was granted".<sup>36</sup> Second, for the sake of uniform interpretation and application of competition policy within the Union, the Commission held that it "cannot be bound by a decision given by a national court in application of Article [101] and [102] of the Treaty."<sup>37</sup>

### **3. FRAND royalty rate determination**

#### **3.1 Meaning of FRAND**

The exact meaning of FRAND remains unclear, nor even after the Commission's *Motorola* FRAND decision. As Swanson and Baumol point out, there are no widely acknowledged tests that could determine whether particular licensing terms do or do not satisfy a FRAND commitment.<sup>38</sup> Apart from demanding that the IPR holders disclose the relevant intellectual property and promise to license their IPRs on FRAND terms once they are essential for implementation of an industry standard, FRAND commitments provided by IPR holders to

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CD-RWs technology – the specifications of which are written on the Orange Book – developed by Philips and Sony. In this case, the German Federal Court ruled on the conditions under which the defendant can raise a competition law defence against an injunction claim. The English translation of the conditions laid down by the German Federal Court could see Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 82.

<sup>33</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 307, 433-464.

<sup>34</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 482-491.

<sup>35</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 465-471.

<sup>36</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 467-468.

<sup>37</sup> Case AT.39985 – Motorola, Commission Decision of 29 April 2014, para 470. See also Judgment in *Masterfoods and HB*, C-344/98, ECLI:EU:C:2000:689, para 48.

<sup>38</sup> See Daniel G. Swanson and William J. Baumol, 'Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power' (2005) 73 *Antitrust Law Journal* 1, p5.

SSOs generally show a considerable lack of definition as to how licensing terms should be concluded to comply with the commitments offered.<sup>39</sup> The FRAND commitments thus could be regarded as “an incomplete contract between licensors and licensees”.<sup>40</sup> The specific licensing terms and conditions including the royalty rates are subject to the negotiation between the IPR holder and the licensee(s).<sup>41</sup> Thus, a FRAND commitment is of limited value to identify whether the licensing terms at issue are FRAND or not.<sup>42</sup> From the perspective of the SSOs, there is no further guidance with regard to the exact meaning of FRAND within their policies (such as ETSI IPR policy<sup>43</sup>, IEEE-SA Standards Board Bylaws<sup>44</sup>). The absence of a concrete definition on the FRAND commitment may, for one thing, secure the widest possible flexibility to establish FRAND terms according to specific situations.<sup>45</sup> From this perspective, licensing freedom provides not only incentives for IPR holders to make their innovations more available, but also the most advantageous licensing terms for the

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<sup>39</sup> See also Anne Layne-Farrar, Jorge A. Padilla and Richard Schmalensee, ‘Pricing Patents for Licensing in Standard-Setting Organizations: Making Sense of FRAND Commitments’ (2007) 74(3) *Antitrust Law Journal* 671, pp.678-679.

<sup>40</sup> Mario Mariniello, ‘Fair, Reasonable and Non-Discriminatory (FRAND) Terms: A Challenge for Competition Authorities’ (2011) 7(3) *Journal of Competition Law and Economics* 523, working paper version, available at SSRN: <http://ssrn.com/abstract=2186052>, last visited on 18 November 2013, p2.

<sup>41</sup> Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, p516. For example, ETSI in its *Guide on IPRs*, section 4.1, holds that: “Specific licensing terms and negotiations are commercial issues between the companies and shall not be addressed within ETSI. Technical Bodies are not the appropriate place to discuss IPR Issues. Technical Bodies do not have the competence to deal with commercial issues. Members attending ETSI Technical Bodies are often technical experts who do not have legal or business responsibilities with regard to licensing issues. Discussion on licensing issues among competitors in a standards making process can significantly complicate, delay or derail this process.” Available at <http://www.etsi.org/images/files/IPR/etsi-guide-on-ipr.pdf>, last visited on 18 November 2013.

<sup>42</sup> Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p5.

<sup>43</sup> The European Telecommunications Standards Institute (ETSI) IPR Policy (Annex 6 of the Rules of Procedure), available at <http://www.etsi.org/images/files/IPR/etsi-ipr-policy.pdf>, last visited on 18 November 2013 and its Guide on IPRs (version adopted by Board #94 on 19 September 2013), available at <http://www.etsi.org/images/files/IPR/etsi-guide-on-ipr.pdf>, last visited on 18 November 2013.

<sup>44</sup> IEEE Standards Association Standards Board Bylaws, approved by the IEEE-SA Board of Governors December 2012, available at [http://standards.ieee.org/develop/policies/bylaws/sb\\_bylaws.pdf](http://standards.ieee.org/develop/policies/bylaws/sb_bylaws.pdf), last visited on 18 November 2013.

<sup>45</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p112. See also Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, p516.

licensees according to their distinguished relationship with the licensor.<sup>46</sup> But for another, the ambiguity in the definition of FRAND is considered to be one of core problems in IPR licensing.<sup>47</sup>

With regard to the elements of ‘fair’ and ‘reasonable’, firstly, it is difficult to make a clear distinction between them. According to some commentators, the element ‘fair’ focuses on the well informed procedure which gives equal consideration to both parties of the licensing, while the element ‘reasonable’ makes sure that the result is acceptable.<sup>48</sup> This interpretation might be questionable, since what raises *ex post* competition concern is whether the licensing terms and conditions are FRAND, but not the process of negotiation. Noting the following two points, it appears that the EU Commission is unwilling to make a clear distinction between them. In the first place, within EU competition law sometimes one element could be replaced by the other. For instance, the *Commission Guidelines on Horizontal Co-operation Agreements* states that “the assessment of whether fees charged for access to IPR in the standard-setting context are *unfair* or *unreasonable* should be based on whether the fees bear a reasonable relationship to the economic value of the IPR.”<sup>49</sup> In the second place, it is questionable whether the element ‘fair’ plays the same role as it played before. It is noteworthy in the *IMS Health* case and *Microsoft I* case that the EU Commission has, by its wording, implicitly replaced the FRAND with the RAND (‘reasonable and non-discriminatory’).<sup>50</sup>

Secondly, it remains unclear what types of transaction terms and conditions are unfair or unreasonable.<sup>51</sup> Apart from excessive pricing which will be discussed in the next section, cases involving other non-monetary transaction terms in EU case law might provide some

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<sup>46</sup> See Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, p516.

<sup>47</sup> Larry M. Goldstein and Brian N. Kearsy, *Technology Patent Licensing: An International Reference on 21<sup>st</sup> Century Patent Licensing, Patent Pools and Patent Platforms* (Aspatore Books, 2004), p27.

<sup>48</sup> See Larry M. Goldstein and Brian N. Kearsy, *Technology Patent Licensing: An International Reference on 21<sup>st</sup> Century Patent Licensing, Patent Pools and Patent Platforms* (Aspatore Books, 2004), pp.27-28.

<sup>49</sup> *Commission Guidelines on Horizontal Co-operation Agreements*, [2011] OJ C11/1, Para 289. (emphasis added)

<sup>50</sup> See *supra* notes **Error! Bookmark not defined.** and **Error! Bookmark not defined.**.

<sup>51</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p112; Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties Standard Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p3; Mark A. Lemley, ‘Intellectual Property Rights and Standard-Setting Organizations’ (2002) 90(6) *California Law Review* 1889, p1964.

guidance. In *Tetra Pak II*<sup>52</sup>, the transaction terms concluded between Tetra Pak and its customers, including limitations placed on the customers' use of the machines, forcing the customers' use of Tetra Pak's repair and maintenance services and surprise inspections right reserved for Tetra Pak, were found to be unfair. In *Amministrazione Autonoma dei Monopoli di Stato* case<sup>53</sup>, the General Court upheld the Commission's decision<sup>54</sup> that it is unfair to impose on foreign cigarettes producers non-negotiable terms, such as limitations on the availability to introduce new brands of cigarettes, maximum quantity of new brands production and monthly production, and restriction on the packaging. In *DSD* case, the General Court<sup>55</sup> and finally the CJEU<sup>56</sup> upheld the Commission's finding in its decision<sup>57</sup>, in which the Commission found DSD concluded trademark agreements with the sale package manufactures and distributors, according to which the customer shall pay service fee in line with the volume of packaging with DSD's logo on them rather than in line with the volume of packaging for which DSD was providing service itself. The Commission ruled that DSD had abused its dominant position on the German packaging collecting market when it claimed the full fees for all the Green Dot logo packaging even the actual service was provided by its competitors.<sup>58</sup> "No service, no fee" is the underlying principle followed by the EU Commission<sup>59</sup>. Although the EU Commission and EU Courts have not explicitly defined the meaning of fairness or reasonableness, it might be thus possible to conclude that, to satisfy the fairness or reasonableness requirement, a dominant undertaking should *not*: 1) exploit its dominant position by imposing irrelevant obligations on its customers, or to conclude license-relevant clause which would not have been reached without such dominant market position; 2) be unjust enriched (e.g. gaining additional profit, maintaining or strengthening market power).<sup>60</sup> The end result should be acceptable to

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<sup>52</sup> Case IV/31043 - *Tetra Pak II*, Commission Decision, [1992] OJ L-72/1. The Commission Decision was upheld by the General Court in the Judgment of 6 October 1994, *Tetrapak v Commission*, T-83/91, ECR, ECLI:EU:T:1994:246, and the Court of Justice in the Judgment of *Tetra Pak*, C-333/94 P, ECLI:EU:C:1996:436.

<sup>53</sup> Judgment of 22 November 2001, *Amministrazione Autonoma dei Monopoli di Stato(AAMS) v. Commission*, T-139/98, ECR, ECLI:EU:T:2001:272.

<sup>54</sup> Case IV/36010-F3 *Amministrazione Autonoma dei Monopoli di Stato*, Commission Decision [1998] OJ L-252/47.

<sup>55</sup> Judgment of 24 May 2007, *Der Grüne Punkt - Duales System Deutschland GmbH v. Commission*, T-289/01, ECR, ECLI:EU:T:2007:155.

<sup>56</sup> Judgment in *Der Grüne Punkt - Duales System Deutschland GmbH*, C-385/07 P, ECLI:EU:C:2009:456.

<sup>57</sup> Case COMP D3/34493, *DSD*, Commission Decision [2001] OJ L166/1.

<sup>58</sup> *Ibid*, Para 100-109.

<sup>59</sup> See the Commission Press IP/01/584, Brussels, 20 April 2001, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/01/584&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 10 November 2013.

<sup>60</sup> As the CJEU put in *United Brands* that "it is advisable to ascertain whether the dominant undertaking has made use of the opportunities arising out of its dominant position in such a way as to reap trading benefits which it



both parties, and should be an outcome that they can live with.<sup>61</sup>

Compared to ‘fair and reasonable’, the ‘non-discriminatory’ element in the FRAND requirement is straightforward and easier to interpret for one thing,<sup>62</sup> but not less important for another.<sup>63</sup> By comparing different licensing conditions, non-discrimination obligation examines whether there are discriminatory conditions that have been applied to equivalent transactions, intending to maintain a level-playing field with respect to actual and potential competition.<sup>64</sup> Apart from distinguished licensing terms, claims of abusive discrimination require evidences of adverse effects on competition.<sup>65</sup> As some commentators observe, “[t]here are a few cases...which allege that a discriminatory price in an intellectual property license is illegal not in and of itself, but rather because it facilitates the exclusion of disfavoured competitors and therefore helps to maintain a monopoly.”<sup>66</sup> Therefore, it would be an abuse of dominant position if an undertaking charges different prices or applies other dissimilar conditions to different customers without proper reason to the extent that the discriminated group of customers are thus unable to compete effectively with others. The dominant undertaking shall bear the burden of proof to justify its different treatments between different customers.<sup>67</sup> The assessment of justification has to be made on the basis of the whole aspects of the case.<sup>68</sup> On the other hand, it may be unnecessary and impractical to treat every party exactly the same.<sup>69</sup> Actually, sometimes the consumers may even benefit from the price

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would not have reaped if there had been normal and sufficiently effective competition.” (Judgment in *United Brands*, 27/76, ECLI:EU:C:1978:22, Para 249)

<sup>61</sup> See Larry M. Goldstein and Brian N. Kearsy, *Technology patent licensing: An International Reference on 21<sup>st</sup> Century Patent Licensing, Patent Pools and Patent Platforms*, (Aspatore, Books: 2004), p27.

<sup>62</sup> See Damien Geradin, ‘The Meaning of “Fair and Reasonable” in the Context of Third-Party Determination of FRAND Terms’ (2014) 21(4) *George Mason Law Review* 919, pp.927-928.

<sup>63</sup> For instance, David J. Teece and Edward F. Sherry argue that the element of ‘non-discriminatory’ should in theory be more important, see David J. Teece and Edward F. Sherry, ‘Standard Setting and Antitrust’ (2003) 87 *Minnesota law Review* 1913, p1956.

<sup>64</sup> See Larry M. Goldstein and Brian N. Kearsy, *Technology patent licensing: An International Reference on 21<sup>st</sup> Century Patent Licensing, Patent Pools and Patent Platforms*, (Aspatore, Books: 2004), pp.27-28.

<sup>65</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p27.

<sup>66</sup> Herbert Hovenkamp, Mark D. Janis and Mark A. Lemley, *IP and Antitrust: An Analysis of Antitrust Principles Applied to Intellectual Property Law* (second edition, Wolters Kluwer, 2013), 13.5d, at 13-61.

<sup>67</sup> See e.g. Judgment in *Minist ère public v Jean-Louis Tournier*, 395/87, ECLI:EU:C:1989:319, Para 38.

<sup>68</sup> See e.g Judgment in *Nederlandsche Banden Industrie Michelin*, 322/81, ECLI:EU:C:1983:313, Para 73.

<sup>69</sup> See Larry M. Goldstein and Brian N. Kearsy, *Technology Patent Licensing: An International Reference on 21<sup>st</sup> Century Patent Licensing, Patent Pools and Patent Platforms* (Aspatore Books, 2004), pp.27-28.

discrimination.<sup>70</sup> Discrimination to some extent should be allowed.<sup>71</sup> As the General Court held in *Microsoft I* that

“The mere fact that the contested decision requires that the conditions to which any licences are subject be reasonable and non-discriminatory does not mean that Microsoft must impose the same conditions on every undertaking seeking such licences. It is not precluded that the conditions may be adapted to the specific situation of each of those undertakings and vary, for example, according to the extent of the information to which they seek access or the type of products in which they intend to implement the information.”<sup>72</sup>

### 3.2 EU rules on excessive pricing

In light of previous analysis, the ambiguously defined FRAND provides little meaningful guidance in the sense that right owners could not rely merely on the concept of FRAND to evaluate whether their setting of royalty rates would violate EU competition rules. It is thus necessary for undertakings to seek other approaches to determine a reasonable royalty, from either a legal or an economic perspective. Against another objective of rapid technology diffusion, the royalty compensation should be properly balanced and provide “a socially optimal incentive” for investment in innovative activities.<sup>73</sup> An unfairly low royalty, which may be unlikely but theoretically possible to occur in a compulsory license subsequent to an abusive refusal to license case, would reduce the incentive of the right owners to continue to invest and to research. Moreover, the licensees’ cost savings from such lower royalties might not give rise to the promotion of end consumers’ welfare, which depends ultimately on the degree of competition on the downstream market.<sup>74</sup> In other words, rather than the level of royalty rates, it is widely accessibility of the essential IPR – which affords certain degree of competition on the downstream market – that would be more relevant with the consumer

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<sup>70</sup> See Benjamin Klein and John S. Wiley, Jr., ‘Competitive Price Discrimination as an Antitrust Justification for Intellectual Property Refusal to Deal’ (2003) 70 *Antitrust Law Journal* 599, pp.611-619; Richard T. Rapp and Lauren J. Stiroh, ‘Standard Setting and Market Power’, statement at the FTC/DOJ hearings on Competition and Intellectual Property Law and Policy in the Knowledge-based Economy, 18 April 2002, available at <http://www.ftc.gov/opp/intellect/020418rappstiroh.pdf>, last visited on 18 November 2013.

<sup>71</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.25-26.

<sup>72</sup> Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 811.

<sup>73</sup> Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.2-3.

<sup>74</sup> See Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, pp.521-522.

welfare.<sup>75</sup>

Compared to the lower royalty rates where concern may arise more from the perspective of protection of incentives on innovative activities investment, the setting of higher royalty rates may cause negative effects on the consumer welfare in the philosophy of EU competition law. It is well acknowledged that US antitrust law does not forbid IPR holders from exploiting their monopoly power to charge monopoly prices from the customers, as long as such conduct is not accompanied by other anti-competitive elements.<sup>76</sup> Judge Posner maintained that “the antitrust laws are not a price-control statute or a public-utility or common-carrier rate-regulation statute”.<sup>77</sup> The US Supreme Court in *Verizon v. Trinko*<sup>78</sup> also confirmed that

“[t]he mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices – at least for a short period – is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth.”<sup>79</sup>

However, on the other side of the Atlantic, once the refusal to license has been deemed as an abuse by the EU Commission, the IPR holders should be cautious in setting the royalty rates. The rates should not be set so high as to constitute a constructive refusal to license in negotiation,<sup>80</sup> or to constitute an excessive pricing under Article 102 TFEU, although not always the case.<sup>81</sup> The EU Commission was reluctant to pursue dominant undertakings’ conducts of charging excessively high prices.<sup>82</sup> This is due to the difficulty in determining at

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<sup>75</sup> Ibid.

<sup>76</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.11-12; The Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights, available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014, p13.

<sup>77</sup> *Blue Cross, et al. v. Marshfield Clinic, et al.*, 65 F.3d 1406, at 1413 (1995).

<sup>78</sup> *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).

<sup>79</sup> Ibid, at 407.

<sup>80</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p113.

<sup>81</sup> Ibid, part G.

<sup>82</sup> See for instance EU Commission’s *Fifth Report on Competition Policy* (1975), available at [http://ec.europa.eu/competition/publications/annual\\_report/ar\\_1975\\_en.pdf](http://ec.europa.eu/competition/publications/annual_report/ar_1975_en.pdf), last visited on 18 November 2013,

which point a price could be considered excessive.<sup>83</sup> However, the Commission turned to condemn practice of excessive pricing if the behaviour is “designed to preserve its dominance, usually directly against competitors or new entrants who would normally bring about effective competition and the price level associated with it”.<sup>84</sup> The EU Commission’s interventionist position in prohibiting excessive pricing could also be seen in the Commission Guidance where it is explicitly provided that “[c]onduct which is directly exploitative of consumers, for example charging excessively high prices [...] that undermines the efforts to achieve an integrated internal market, is also liable to infringe Article [102]”.<sup>85</sup> The Commission’s on-going investigation against Russian energy giant Gazprom demonstrates that the EU competition top enforcer is still pursuing excessive pricing, as in that investigation one of the suspected anti-competitive practices is that Gazprom may have imposed unfairly high prices on its customers in Central and Eastern Europe.<sup>86</sup>

The Court of Justice in the *United Brands* case held that “charging a price which is excessive because it has no reasonable relation to the economic value of the product supplied would be such an abuse.”<sup>87</sup> Subsequently, the CJEU restated that an undertaking abuses its dominant position where it charges excessive services fees which have no reasonable relation to the economic value of the service provided in a number of cases, such as *General Motors*,<sup>88</sup> *British Leyland*,<sup>89</sup> *Centre d'Insémination de la Crespelle*,<sup>90</sup> *GT-Link*,<sup>91</sup> *TNT*<sup>92</sup> And *DSD*.<sup>93</sup>

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point 3 at p13. (“[M]easures to halt the abuse of dominant positions cannot be converted into systematic monitoring of prices. In proceedings against abuse consisting of charging excessively high prices, it is difficult to tell whether in any given case an abusive price has been set for there is no objective way of establishing exactly what price covers costs plus a reasonable profit margin.”)

<sup>83</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p150; Alison Jones and Brenda Sufrin, *EC Competition Law: text, cases, and materials* (3<sup>rd</sup> edition, Oxford University Press, 2007), p588.

<sup>84</sup> The EU Commission’s XXIVth Report on Competition Policy (1994), available at [http://bookshop.europa.eu/is-bin/INTERSHOP.enfinity/WFS/EU-Bookshop-Site/en\\_GB/-/EUR/ViewPublication-S tart?PublicationKey=CM9095283](http://bookshop.europa.eu/is-bin/INTERSHOP.enfinity/WFS/EU-Bookshop-Site/en_GB/-/EUR/ViewPublication-S tart?PublicationKey=CM9095283), last visited on 18 November 2013, point 207 at p120.

<sup>85</sup> Communication from the Commission – *Guidance on the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings*, [2009] OJ C45/7, Para 7.

<sup>86</sup> EU Commission Press release at [http://europa.eu/rapid/press-release\\_IP-12-937\\_en.htm](http://europa.eu/rapid/press-release_IP-12-937_en.htm), last visited on 8 June 2014.

<sup>87</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 250. (emphasis added)

<sup>88</sup> Judgment in *General Motors*, 26-75, ECLI:EU:C:1975:150, Para 12.

<sup>89</sup> Judgment in *British Leyland*, 226/84, ECLI:EU:C:1986:421, Para 27.

<sup>90</sup> Judgment in *Société Civile Agricole du Centre d'Insémination de la Crespelle v. Coopérative d'Elevage et d'Insémination Artificielle du Département de la Mayenne*, C-323/93, ECLI:EU:C:1994:368, Para 25.

As to the appropriate remuneration for use of the protected subject matter of the IP at issue, it is clear from settled case law – such as *FDV*<sup>94</sup>, *Kanal 5 and TV 4*,<sup>95</sup> and *FAPL*<sup>96</sup> – that the remuneration must also be reasonable in relation to the economic value of the service provided. More specifically, in the follow-on *Microsoft* case (*‘Microsoft II’*), the General Court upheld the Commission’s decision, declaring that a reasonable remuneration charged should only reflect the *intrinsic value* of the technologies rather than the *strategic value* stemming from the IPR holder’s market power.<sup>97</sup> Nevertheless, the General Court did not require the Commission to choose a particular royalty rate and impose that upon Microsoft,<sup>98</sup> and added that “the use of imprecise legal concepts within a provision does not prevent liability being established”.<sup>99</sup>

With regard to the analytical framework to assess whether a high price could be qualified as an excessive price under Article 102 TFEU, the CJEU in *United Brands* formulated a two-step approach: firstly, whether the difference between the costs incurred and the price charged is excessive, and secondly if the answer to the first step is affirmative whether the price charged is unfair either in itself or compared to competing products.<sup>100</sup> The CJEU made it clear in *Isabella Scippacercola and Ioannis Terezakis*<sup>101</sup> that the two prongs of the second step of the *United Brands* test are not cumulative but parallel.<sup>102</sup> The EU Commission in the significant excessive pricing case *Port of Helsingborg*, for one thing, applied the *United*

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<sup>91</sup> Judgment in *GT-Link A/S v. De Danske Statsbaner (DSB)*, C-242/95, ECLI:EU:C:1997:376, Para 39.

<sup>92</sup> Judgment in *TNT Traco SpA v Poste Italiane SpA and Others*, C-340/99, ECLI:EU:C:2001:281, Para 46.

<sup>93</sup> Judgment in *Der Grüne Punkt - Duales System Deutschland GmbH*, C-385/07 P, ECLI:EU:C:2009:456, Para 142.

<sup>94</sup> Judgment in *Foreningen af Danske Videogramdistributører v Laserdisker*, C-61/97, ECLI:EU:C:1998:422, Para 15.

<sup>95</sup> Judgment in *Kanal 5 and TV 4*, C-52/07, ECLI:EU:C:2008:491, Para 36-38.

<sup>96</sup> Judgment in *Football Association Premier League Ltd and others v QC Leisure and others*, C-403/08 and C-429/08, ECLI:EU:C:2011:631, Para 109.

<sup>97</sup> Case COMP/C-3/37792 *Microsoft*, Commission Decision of 27 February 2008, Para 106, 107; Judgment of 27 June 2012, *Microsoft v Commission*, T-167/08, ECR, ECLI:EU:T:2012:323, Para 138, 142-144, 149, 150.

<sup>98</sup> Judgment of 27 June 2012, *Microsoft v Commission*, T-167/08, ECR, ECLI:EU:T:2012:323, Para 95.

<sup>99</sup> *Ibid*, Para 91.

<sup>100</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 251-252. See also Joaquín Almunia, Vice president of the European Commission responsible for competition policy, speech ‘Abuse of Dominance: A View from the EU’, at the *Fordham’s Competition Law Institute Annual Conference*, New York, 27 September 2013, available at [http://europa.eu/rapid/press-release\\_SPEECH-13-758\\_en.htm?locale=en](http://europa.eu/rapid/press-release_SPEECH-13-758_en.htm?locale=en), last visited on 17 November 2013.

<sup>101</sup> Order of the Court of Justice in *Isabella Scippacercola and Ioannis Terezakis*, C-159/08 P, ECLI:EU:C:2009:188.

<sup>102</sup> *Ibid*, Para 47.

*Brands* two-step approach.<sup>103</sup> For another, for concluding that the price charged bears no relation to the economic value of the service provided, the Commission has adopted a high standard of proof by taking into account a wide range of tangible and intangible factors, such as demand-side aspects, initial investment, intangible value and opportunity cost.<sup>104</sup>

However, the *United Brands* two-fold approach appears to be not applicable in the context of IP licensing. In the first step, the cost-price comparison depends on a comprehensive cost analysis, which is not easy even in non-IP situations. The Court of Justice in *United Brands* judgment admitted that it is very difficult “in working out production costs which may sometimes include a discretionary apportionment of indirect costs and general expenditure and which may vary significantly according to the size of the undertaking, its object, the complex nature of its set up, its territorial area of operations, whether it manufactures one or several products, the number of its subsidiaries and their relationship with each other.”<sup>105</sup> In addition, it is almost impossible to ascertain the costs of an efficient firm in a given market in cases where lack of competition resulted into that the dominant undertaking had no incentive to keep costs down.<sup>106</sup> Further, it would be extremely difficult, if not impossible, when intellectual property is involved.<sup>107</sup> As pointed out by some scholars, the IPR system should be something analogous to the rationale of lottery in the sense that the system “[forces] inventors to bear their own losses from failure but [holds] out the prospect of monopoly in the event of success.”<sup>108</sup> Apart from the costs in the successful research activities, as the reward for the innovatory and risk-taking activity of the IPR holder, the price-cost analysis should guarantee that the licensing fee could at least cover the IPR holder’s sunk costs – the past research costs incurred in the failed R&D activities that did not result in commercially exploitable products, and the significant transaction costs. The latter may cover the licensor’s expenditures relevant to the IPR license such as the costs of negotiation, contracting, accounting, monitoring and auditing, the costs of instruction, training and 24-hour assistance,

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<sup>103</sup> Case COMP/A.36.568/D3 – *Scandlines Sverige AB v. Port of Helsingborg*, Commission decision on 23 July 2004, Para 146, 147. (*Scandlines Sverige AB* brought an action against the decision of the Commission, Case T-399/04, which is still pending).

<sup>104</sup> *Ibid*, Para 209, 226, 227, 234.

<sup>105</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, para 254.

<sup>106</sup> See Damien Geradin, ‘The Necessary Limits to the Control of “Excessive” Prices by Competition Authorities – A View from Europe’, Tilburg University Legal Studies Working Paper, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1022678](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1022678), last visited on 10 October 20014, p8.

<sup>107</sup> See Michal S. Gal, ‘Monopoly pricing as an antitrust offence in the U.S. and the EC: two systems of belief about monopoly?’ (2004) 49 *Antitrust Bulletin* 343, p369.

<sup>108</sup> Phillip Areeda and Louis Kaplow, *Antitrust Analysis: Problems, Text, Cases* (5<sup>th</sup> edition, Aspen Publishers, 1997), p430.

and the costs of upgrading.<sup>109</sup> Furthermore, cost is not the sole factor in the calculation of a reasonable price. According to the Commission, the economic value “cannot simply be determined by adding a profit margin to the approximate costs incurred in the provision of a product or service”.<sup>110</sup> Rather, the economic value must be determined “with regard to the particular circumstances of the case and take into account also non-cost-related factors”.<sup>111</sup> Therefore, the difficulty in calculating relevant costs results in that it might be right to conclude that the cost-based approach is no longer well adapted to the context of IP licensing.<sup>112</sup>

Even if the costs incurred could be theoretically calculated in the first step, the second step of the *United Brands* test is also inapplicable in IP-related cases, especially in follow-up refusal to license scenario. As to the first prong that assesses whether the high price is unfair in itself, it is not possible to quantify a reasonable profit margin, or a “just reward” for the creative effort in reconstructing a fair price.<sup>113</sup> In the context of IPR royalty determination, the value

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<sup>109</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p22.

<sup>110</sup> Case COMP/A 36.568/D3, *Scandlines Sverige AB v. Port of Helsingborg*, Commission Decision of 23 July 2004, Para. 232.

<sup>111</sup> *Ibid.*

<sup>112</sup> *Commission Guidelines on Horizontal Co-operation Agreements*, *supra* note 49, the Commission in Para 289 argues that “[i]n principle, cost-based methods are not well adapted to this context because of the difficulty in assessing the costs attributable to the development of a particular patent or groups of patents.” The Commission then extends to suggest that “it may be possible to compare the licensing fees charged by the company in question for the relevant patents in a competitive environment before the industry has been locked into the standard (*ex ante*) with those charged after the industry has been locked in (*ex post*).” On the choice of *ex ante/ex post* royalty rates, some commentators suggest that a reasonable royalty should be the royalty in determining which IPR owner’s market power established by standardisation has not been exercised, or a reasonable royalty should be established on an *ex ante* basis. See for instance Carl Shapiro and Hal R. Varian, *Information Rules: A Strategic Guide to the Network Economy* (Harvard Business School Press, 1999), p241; Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties Standard Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p5. On the contrary, there are other commentators who maintain that standardisation should not deprive an IPR owner of his right to accept the price that the market is willing to pay, therefore the actual level of royalties should be left for the licensor and licensee(s) to decide. According to these authors, the license would be considered fair and reasonable if the terms are concluded “in arm’s-length negotiations”. See for instance Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, pp.114-115; Ilkka Rahnasto, *Intellectual Property Rights, External Effects and Anti-trust Law: Leveraging IPRs in the Communications Industry* (Oxford University Press, 2003), Para 4.105 and Para 6.34.

<sup>113</sup> Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), p259; Fritz Machlup, ‘An Economic Review of the Patent System’, Study of the Committee on Patents, Trademarks, and

of inspiration – “flashes of creative brilliance from which every invention springs”, which should be taken into account, given its nature however is impossible to be determined by any court.<sup>114</sup> As to the second prong in the second step that determines price excessiveness by conducting price comparison between the dominant undertaking’s product and the competing products,<sup>115</sup> the difficulty in IP-related cases apparently lies in finding genuinely comparable licensing fees.<sup>116</sup> It might be particularly unpractical to conduct such a comparison in the follow-up refusal to license cases, where there are no effectively competitive IPRs within the relevant market and accordingly it is impossible to determine how much the IPR holder has reaped that he would not have obtained in a competitive market.<sup>117</sup> Additionally, take a step back, comparing different licenses is quite difficult, if not impossible, since IPRs in general are highly differentiated.<sup>118</sup> This may to some extent explain why the EU Commission has not outlined in the FRAND cases what a reasonable royalty rate should be, but only declared that “courts and arbitrators are well-placed to set FRAND rates in cases of disputes”.<sup>119</sup>

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Copyright Committee on the Judiciary, US Senate, 85<sup>th</sup> Congress, Study No. 15, Washington, 1958, p12. The US practitioners also made it clear in the Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights (available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014) that “even if one could analyze the costs of developing an IPR, there is no framework to provide an adequate definition of an ‘unfair’ price in the IPR context” (at p13).

<sup>114</sup> Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, pp.154-155. See also Maurits Dolmans, ‘Standards for Standards’ (2002) 26(1) *Fordham International Law Journal* 163, pp.201-202.

<sup>115</sup> As to the possibility of comparing the price charged by the dominant undertaking with those of other products, Liyang Hou summarizes six types of benchmarking in his paper, see Liyang Hou, ‘Excessive Prices within EU Competition Law’ (2011) 7(1) *European Competition Journal* 47, pp.63-69.

<sup>116</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p155.

<sup>117</sup> See Inge Govaere, *The Use and Abuse of Intellectual Property Rights in E.C. Law* (Sweet & Maxwell 1996), pp.259-260.

<sup>118</sup> See the Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights, available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014, p13.

<sup>119</sup> See EU Commission press release at [http://europa.eu/rapid/press-release\\_MEMO-14-322\\_en.htm](http://europa.eu/rapid/press-release_MEMO-14-322_en.htm), last visited on 8 June 2014.



As required by the EU Commission in *Microsoft I*, the software giant should “make the Interoperability Information available to *any undertaking having an interest* in developing and distributing work group server operating system products”.<sup>120</sup> The licensing terms and conditions might also be affected by the fact whether the IPR holder negotiates with each licensee separately, or the IPR holder enters into a collective negotiation with a number of licensees. Unlike the bilateral negotiations that bring certain degree of competition between the licensees on the downstream market, collective negotiations would likely lead to homogenization of the licensing conditions, i.e. charging a similar license fee to the licensees regardless of their unequal situations in the marketplace.<sup>121</sup> Such ‘one-size-fits-all’ negotiation results disallowing efficient discrimination in licensing conditions might involve collusion between competing undertakings in the relevant market under Article 101(1) TFEU, and diminish the competition thereof.<sup>122</sup> In general, collaboration among the potential buyers may allow those competing entities “to centralize ordering, to combine warehousing or distribution functions more efficiently, or to achieve other efficiencies.”<sup>123</sup> But it seems that such efficiency-enhancing effect is unlikely to apply in IPR licensing context since the bargaining power from the licensees’ side is inadequate to lower the royalty rates. Therefore, in terms of the monetary compensation, IPR owner’s incentive to invest and innovate would, compared to bilateral negotiations, not be diminished in collective negotiations. Additionally, there is no evidence demonstrating that end consumers would benefit from the cost savings (if any),<sup>124</sup> resulting from, for instance, the collective negotiations.

### 3.3 Selected economic models

Given the fact that the EU approach from the perspective of excessive pricing<sup>125</sup> has not

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<sup>120</sup> Case COMP/C-3/37.792, *Microsoft*, *supra* note **Error! Bookmark not defined.**, Article 5(a). (emphasis added)

<sup>121</sup> See Damien Geradin and Miguel Rato, ‘Can Standard-Setting Lead to Exploitative Abuse? A Dissonant View on Patent Hold-up, Royalty Stacking and the Meaning of FRAND’ (2007) 3(1) *European Competition Journal* 101, p134. See also Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, pp.525-526.

<sup>122</sup> *Ibid.*

<sup>123</sup> U.S. Department of Justice and Federal Trade Commission, *Antitrust Guidelines for Collaborations among Competitors* (2000), available at <http://www.ftc.gov/os/2000/04/ftcdojguidelines.pdf>, last visited on 18 November 2013, p14.

<sup>124</sup> See Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, pp.521-522.

<sup>125</sup> It should be noted that in the US the courts have addressed the reasonable royalty rates determination issue in IP infringement lawsuits. The primary US case guiding reasonable royalty rates setting *Georgia-Pacific v. United States* put forward a comprehensive list of fifteen IP licensing-related factors, “[a] comprehensive list of

formulated an exactly clear and predictable test for IPR holders to determine a reasonable royalty rate, this section turns to models in economics literature and intends to examine whether these economic models are capable of providing benchmarks for a FRAND royalty rate. Economists have debated for decades and have proposed a number of economic approaches to calculate a reasonable royalty rate. Considering the complexity involved in these models and their relevance to the subject of this research, this section selects the Lemley-Shapiro model, the Swanson-Baumol model and the Epstein-Marcus model, and discusses how a reasonable royalty rate is determined in each model by adopting different

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evidentiary facts relevant, in general, to the determination of the amount of a reasonable royalty for a patent license may be drawn from a conspectus of the leading cases. The following are some of the factors *mutatis mutandis* seemingly more pertinent to the issue herein: 1. The royalties received by the patentee for the licensing of the patent in suit, proving or tending to prove an established royalty. 2. The rates paid by the licensee for the use of other patents comparable to the patent in suit. 3. The nature and scope of the license, as exclusive or non-exclusive; or as restricted or non-restricted in terms of territory or with respect to whom the manufactured product may be sold. 4. The licensor's established policy and marketing program to maintain his patent monopoly by not licensing others to use the invention or by granting licenses under special conditions designed to preserve that monopoly. 5. The commercial relationship between the licensor and licensee, such as, whether they are competitors in the same territory in the same line of business; or whether they are inventor and promotor. 6. The effect of selling the patented specialty in promoting sales of other products of the licensee; the existing value of the invention to the licensor as a generator of sales of his non-patented items; and the extent of such derivative or convoyed sales. 7. The duration of the patent and the term of the license. 8. The established profitability of the product made under the patent; its commercial success; and its current popularity. 9. The utility and advantages of the patent property over the old modes or devices, if any, that had been used for working out similar results. 10. The nature of the patented invention; the character of the commercial embodiment of it as owned and produced by the licensor; and the benefits to those who have used the invention. 11. The extent to which the infringer has made use of the invention; and any evidence probative of the value of that use. 12. The portion of the profit or of the selling price that may be customary in the particular business or in comparable businesses to allow for the use of the invention or analogous inventions. 13. The portion of the realizable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer. 14. The opinion testimony of qualified experts. 15. The amount that a licensor (such as the patentee) and a licensee (such as the infringer) would have agreed upon (at the time the infringement began) if both had been reasonably and voluntarily trying to reach an agreement; that is, the amount which a prudent licensee -- who desired, as a business proposition, to obtain a license to manufacture and sell a particular article embodying the patented invention -- would have been willing to pay as a royalty and yet be able to make a reasonable profit and which amount would have been acceptable by a prudent patentee who was willing to grant a license.” (*Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116, at 1120 (SDNY 1970)). Judge Robart in *Microsoft Corp. v. Motorola, Inc.*, No. C 10-1823JLR, 2013 WL 2111217 (W.D. Wa. Apr. 25, 2013), and Judge Holderman in *In re Innovatio IP Ventures, LLC Patent Litig.*, MDL No. 2303, 2013 WL 5593609 (N.D. Ill. Oct. 3, 2013) have adopted a modified-version of the *Georgia-Pacific* factors to recreate a hypothetical negotiation between the parties. In the modified approach, the US courts consider, *inter alia*, the importance of the SEPs to the standard at issue, the importance of the standard and the SEPs to the products at issue, and other comparable patents as benchmarks.

variables.<sup>126</sup>

### 3.3.1 The Lemley–Shapiro model

The Lemley-Shapiro economic model proposes to determine a reasonable royalty rate in the situation where the IPR holder alleges a downstream producer has infringed his IPR. Lemley and Shapiro firstly define some economic variables which are used in the model as follows<sup>127</sup>:

- $V$  is the value enhanced or the cost reduced per unit of the final product by incorporating the IPR at issue;
- $B$  is the bargaining skill of the IPR holder, as measured by the percentage of the gains captured by the IPR holder from the licensing negotiation, ranging from 0 to 1;
- $\theta$  is the strength of the IPR at issue – which might vary during the process of negotiation and litigation in a more complex model,<sup>128</sup> as measured by the likelihood that the result of the IPR infringement lawsuit will be in favour of the IPR holder in the sense that the IPR is found valid and it has been infringed by the

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<sup>126</sup> Other approaches, which are not elaborated in this section, include, for instance: Layne-Farrar, Padilla and Schmalensee's Cooperative Game-Theoretic approach, which is based on dividing rents in cooperative groups originally derived by Lloyd S. Shapley in 1953, see Anne Layne-Farrar, A. Jorge Padilla and Richard Schmalensee, 'Pricing Patents for Licensing in Standard-Setting Organizations: Making Sense of FRAND Commitments' (2007) 74 *Antitrust Law Journal* 671, pp.693-705; Mariniello's screening test with four conditions to assess whether a violation of FRAND occurs, see Mario Mariniello, 'Fair, Reasonable and Non-Discriminatory (FRAND) Terms: A Challenge for Competition Authorities' (2011) 7(3) *Journal of Competition Law and Economics* 523. With regard to the allocation of royalties among standard-essential patents owners in the standard-setting context, it should be noted that in the complaints against Qualcomm in EU, the complainant proposed a 'numeric proportionality rule' to determine the level of royalties, arguing that the allocation of royalties among patent owners should be proportional to the number of essential patents that contributed to the standard. However, Layne-Farrar, Padilla and Schmalensee argue that the 'numeric proportionality rule' is only suitable in a limited set of circumstances due to a number of its disadvantages. It appears this approach merely addresses the concern as to how to divide the royalties charged among the contributors who incorporated their IPR into a standard, but does not provide any guidance on determining a reasonable royalty rate. See Anne Layne-Farrar, Jorge A. Padilla and Richard Schmalensee, 'Pricing Patents for Licensing in Standard-Setting Organizations: Making Sense of FRAND Commitments' (2007) 74(3) *Antitrust Law Journal* 671, pp.683-685. On this subject, the *Commission Guideline on Horizontal Co-operation Agreements*, *supra* note 49, in Para. 290 suggests that an independent expert assessment of the objective centrality and essentiality of the standard at issue of the relevant IPR portfolio, *ex ante* disclosures of licensing terms in the context of a specific standard-setting process, or the royalty rates charged for the same IPR in other comparable standards could serve as appropriate indications.

<sup>127</sup> See Mark Lemley and Carl Shapiro, 'Patent Holdup and Royalty Stacking' (2007) 85 *Texas Law Review* 1991, pp.1996-1997.

<sup>128</sup> *Ibid*, fn.11.

downstream competitor;

- $M$  is the margin, or the profit earned per unit;
- $C$  is the proportion of the cost incurred in the downstream producer's redesigning its product to avoid infringing the IPR at issue, in the total value of the final product;
- $L$  is the proportion of the total sales lost of the downstream producer expected during the IPR lifetime if the producer is excluded from the market by an injunction.

Lemley and Shapiro firstly set up the benchmark level for the royalty rate. If the IPR at issue is certainly valid, the benchmark royalty rate should take into account the value of the IPR for the downstream production and the IPR holder's bargaining skill, namely the rate should be the result of  $B \times V$ .<sup>129</sup> If it is not certain whether the validity of the IPR at issue will be confirmed by a court decision, the benchmark royalty rate should be equal to the result of  $\theta \times B \times V$ .<sup>130</sup> In other words, the royalty rate should consider as well the probability that the licensor possesses a valid IPR and could win the IPR infringement case, thus the reward for the IPR holder should be proportional to the IPR strength.<sup>131</sup>

The benchmark royalty rate, according to the authors, is not designed for replacing the negotiated royalty rate, since there is a "royalty overcharge" gap between the former and the latter.<sup>132</sup> The amount of such royalty overcharge varies according to the downstream producer's strategy choice in negotiating with the IPR holder. The downstream producer could, either choose wait-and-see strategy and redesign his product only if he loses the IPR infringement case ('Litigate Strategy'), or choose to develop a backup version of his product during the litigation ('Redesign and Litigate Strategy')<sup>133</sup>. The 'litigate strategy' will normally be employed if the licensee considers the validity of the IPR at issue is weak, while the 'redesign and litigate strategy' will be adopted if he considers the IPR is strong. If the downstream producer chooses to adopt the 'litigate strategy', the percentage of the overcharged royalty rate should reflect the downstream producer's expenses on redesigning his product and his sales lost due to the injunction, so the percentage gap should be defined as  $C + \frac{M-V}{V} \times L$ .<sup>134</sup> It is important to remind that the further the margins ( $M$ ) are in excess of the value of the IPR at issue ( $V$ ), the more the downstream producer will lose on that market before he redesigns his product. In this case, based on the previous benchmark royalty rate,

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<sup>129</sup> Ibid, p1999.

<sup>130</sup> Ibid.

<sup>131</sup> Ibid, pp.1999-2000.

<sup>132</sup> Ibid, p2000.

<sup>133</sup> Ibid.

<sup>134</sup> Ibid, p2001.

the negotiated royalty rate should be the result of  $\theta \times B \times V \times (1 + C + \frac{M-V}{V} \times L)$ .

On the other hand, if the downstream producer chooses the ‘redesign and litigate strategy’ – namely redesigning his product during the process of the IPR infringement litigation in order to avoid the risk of losing the market sales, the percentage of the overcharged royalty rate should be calculated differently. Unlike the ‘litigate strategy’, the downstream producer in this situation will not be forced off the market, so there is no market sales lost. Another difference that could be observed is that the IPR strength should be taken into account in measuring the costs of redesigning the product. Because in this case the litigation is still on-going, while in the ‘Litigate Strategy’ the costs of redesigning occurs only when the downstream producer loses his case. Therefore the percentage of the overcharged royalty rate, according to Lemley and Shapiro, should be equal to  $\frac{C}{\theta}$ .<sup>135</sup> The rationale here is that more likely the IPR is found invalid or not infringed by a court decision, more money will be wasted on the part of the downstream producer on redesigning his product.<sup>136</sup> Thus the negotiated royalty rate would be the result of  $\theta \times B \times V \times (1 + \frac{C}{\theta})$ .

The key point Lemley and Shapiro have stressed in their analysis is that, IPR should be something probabilistic as opposed to certain. Therefore, the authors argue that, compared to the proposed negotiated royalty rate out of court, the court-based rules, such as the *Georgia – Pacific factors*, would result in an overcharged rate on the grounds that the IPR strength has not been taken into consideration.<sup>137</sup> In the court-based rules there are other problems that drive the royalty rates up in favour of the IPR holders. The problem could be the reliance on other royalty rates in the same industry, since other royalty rates might already exceed the reasonable rates.<sup>138</sup> This might result in a degree of circularity, which is even more apparent if the first court-determined rate infects all subsequent royalty rates.<sup>139</sup> The problem could also originate from the ill-informed experts, whose source of available information about industry royalty rate overestimates the reasonable royalty rate.<sup>140</sup> Moreover, the problem could derive from the calculation of the value of the IPR at issue *V*. The value of the IPR

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<sup>135</sup> Ibid, p2002.

<sup>136</sup> Ibid.

<sup>137</sup> Ibid, pp.2019-2020. See also Daralyn J. Durie and Mark A. Lemley, ‘A Structured Approach to Calculating Reasonable Royalties’ (2010) 14(2) *Lewis & Clark Law Review* 627, p642.

<sup>138</sup> See Mark Lemley and Carl Shapiro, ‘Patent Holdup and Royalty Stacking’ (2007) 85 *Texas Law Review* 1991, pp.2021-2022.

<sup>139</sup> Ibid.

<sup>140</sup> Ibid, pp.2022-2023.

should be based on the contribution of the IPR as a component to the final product, rather than on the price of the entire downstream product. It is however difficult, either to separately observe the value of the IPR at issue, or to determine the contribution of other inputs to the final product other than the IPR input (in the latter approach the value of the IPR at issue could be the result of the price of the entire final product less the value of other inputs).<sup>141</sup>

### 3.3.2 The Swanson–Baumol model

According to Swanson and Baumol, a FRAND royalty rate should strike a balance between the licensor and the licensee's interests, and provide benefits to both parties "by offering *the licensee* all of that portion of the total profits that is made possible by any superiority in its efficiency in utilization of the IP in question, and by ensuring *the licensor* at least as much profit as it could obtain through refusal to license."<sup>142</sup> The Swanson-Baumol model is divided into two parts: the *ex ante* auction for the requirement of 'reasonable' and the Efficient Component Pricing Rule for the requirement of 'non-discriminatory', the choice of which depends on the fact whether the IPR holder is a vertically integrated undertaking.<sup>143</sup>

#### (1) 'Reasonable' requirement: *ex ante* auction

Swanson and Baumol advocate that, to avoid an excessive royalty rate resulting from the IPR holder's exercise of its market power, a reasonable level of royalty rate could be determined through an auction-like process before the standard selection in the situation where the IPR holders are not manufacturers of the final product on the downstream market.<sup>144</sup> Such an auction-like process within the SSOs is conducted when the market is still competitive, namely before one or more IPRs are selected by the SSOs to be the industry standard. In such *ex ante* auction, competing IPR holders simultaneously submit their FRAND commitments and their "best and final" detailed licensing terms to the SSOs.<sup>145</sup> Then the potential licensees on the downstream market could choose their preferred IPR offered by the competing

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<sup>141</sup> Ibid, pp.2021, 2023-2025.

<sup>142</sup> Daniel G. Swanson and William J. Baumol, 'Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power' (2005) 73 *Antitrust Law Journal* 1, p6.

<sup>143</sup> Layne-Farrar, Padilla and Schmalensee propose to extend this model to the situations where standards consist of several or many IP contributions held by multiple parties, and analyze the determination of FRAND rates under five alternative scenarios. See Anne Layne-Farrar, Jorge A. Padilla and Richard Schmalensee, 'Pricing Patents for Licensing in Standard-Setting Organizations: Making Sense of FRAND Commitments' (2007) 74(3) *Antitrust Law Journal* 671, pp.688-693.

<sup>144</sup> See Daniel G. Swanson and William J. Baumol, 'Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power' (2005) 73 *Antitrust Law Journal* 1, pp.15-21.

<sup>145</sup> Ibid, pp.16-17.

licensors with lowest royalty rate and other favourable licensing terms. To demonstrate how a reasonable royalty rate per unit of the downstream market product is derived from the auction-like process, Swanson and Baumol make a number of assumptions to confine their analysis into a simplified scenario where there is no recurring costs such as the costs for further development, technical support or licensing contract management, where the choice made by the potential licensees has nothing to do with the product quality but only (equally) affects their production costs.<sup>146</sup> If all the information required has been disclosed timely and sufficiently, the reasonable royalty rate could be obtained by comparing the difference of the production costs per unit between the ‘best’ IPR (with the lowest production costs for the downstream production) and the ‘next-best’ IPR (with the second lowest production costs for the downstream production). For example, if the ‘best’ IPR A would cause production costs  $X$  per unit of final output and the ‘next-best’ IPR B would cause per unit production costs  $Y$  ( $Y > X$ ), then IPR A’s holder – if he is reasonable enough – will set the royalty rate less than the result of  $(Y - X)$  to ensure that the potential licensees will select his IPR as downstream input. Thus, the total costs incurred for the downstream producers who use IPR A will be less than  $Y$  (production costs  $X$  + maximum royalty rate  $(Y - X) = Y$ ), which is lower than using IPR B or other competing IPRs.<sup>147</sup>

Swanson and Baumol also extend their analysis to a more realistic situation – still simplified though – in which recurring costs (namely “the incremental cost of recurring innovation and licensing expenses”) have been taken into account.<sup>148</sup> According to Swanson and Baumol, if each IPR holder incurs identical recurring costs, let us say  $Z$ , then it is obvious that in the first place for each IPR holder the reasonable royalty rate should cover the recurring costs  $Z$ .<sup>149</sup> As to the ‘best’ IPR A, the maximum royalty rate charged by the holder could be the recurring costs  $Z$ , plus the difference of production costs incurred between adopting such ‘best’ IPR and the ‘next-best’ IPR on the downstream market. In other words, it is possible that reasonable royalty rate ranges from the recurring costs  $Z$ , to the sum of the recurring costs and the difference in value between the ‘best’ IPR A and the ‘next-best’ IPR B, which is  $Z + (Y - X)$ . When the ‘next-best’ IPR B or any other competing IPR (C, D, E, ...) comes closer to being perfect substitute to the ‘best’ IPR A and the difference of production costs approaches zero (in the case of IPR B, the result of  $Y - X$  comes closer to zero), then the reasonable royalty

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<sup>146</sup> Ibid, pp.18-19.

<sup>147</sup> Ibid, p19.

<sup>148</sup> Ibid, p19.

<sup>149</sup> Ibid, p19.

rate would be close to  $Z$ , the recurring costs.<sup>150</sup>

## **(2) ‘Non-discriminatory’ requirement: Efficient Component Pricing Rule (‘ECPR’)**

On the other hand, it is not common that these non-vertically integrated IPR holders would be incentivized to discriminate in licensing with its anti-competitive reasons.<sup>151</sup> The incentives of vertically integrated IPR holders to squeeze out its competitors and strengthen its market power on the downstream market serve as the only plausible explanation for such discriminatory licensing conduct.<sup>152</sup> Therefore, compared to the approach to defining a reasonable royalty rate, the case of a pure IPR holder is not suitable in interpreting the requirement of ‘non-discriminatory’. Considering that either a too high, or a too low royalty rate would cause inefficiencies and increase social costs in the process of final product manufacturing, Swanson and Baumol consider that the solution could be that all the IPR implementers, including the vertically integrated IPR holder itself, are charged equally for using the IPR at issue.<sup>153</sup> It means that the implicit royalty rate the IPR holder charges itself should be equal to the royalty rate paid by the licensees. Then, no matter which course the IPR holder chooses, the profits deriving from the IPR would be exactly the same. If so, the IPR holder would be indifferent between producing the downstream market product itself and licensing its IPR to the rivals in the downstream market to produce the final product.<sup>154</sup> However, the difficulty lies in that, compared to the easily observable royalty rates charged to the rivals, the implicit royalty rate the IPR holder charges itself is not easily identified since a license price in the IPR holder’s accounting documents might be artificial and useless.<sup>155</sup> Swanson and Baumol thus describe the latter as the “money [moving] from one of the firm’s pockets to another”.<sup>156</sup>

To define a non-discriminatory royalty rate, Swanson and Baumol base their economic model on the ‘efficient component pricing rule’ (‘ECPR’), which is both necessary and sufficient for

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<sup>150</sup> Ibid, p19 and p23.

<sup>151</sup> Ibid, pp.26-27.

<sup>152</sup> Herbert Hovenkamp, Mark D. Janis and Mark A. Lemley, *IP and Antitrust: An Analysis of Antitrust Principles Applied to Intellectual Property Law* (second edition, Wolters Kluwer, 2013), 13.5d, at 13-62.

<sup>153</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, p29.

<sup>154</sup> Ibid, pp.36-37. See also Anne Layne-Farrar, Jorge A. Padilla and Richard Schmalensee, ‘Pricing Patents for Licensing in Standard-Setting Organizations: Making Sense of FRAND Commitments’ (2007) 74(3) *Antitrust Law Journal* 671, p687.

<sup>155</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.28-29.

<sup>156</sup> Ibid, p29.



getting a competitively neutral royalty rate. In Swanson and Baumol's words, "*any license fee that substantially departs from the ECPR level can be deemed to violate the [F]RAND requirement of nondiscrimination*".<sup>157</sup> The implicit royalty rate the IPR holder charges itself should equal the price of the final product incorporating the requested IPR less the IPR holder's incremental costs of all remaining inputs, and this rule could be expressed as the equation below:

$$(1) P_i = P_{f,i} - IC_{r,i}$$

(Where  $P_i$  = the royalty rate charged by IPR holder  $i$  per unit of downstream product,  $P_{f,i}$  = the price of the downstream product incorporating the IPR concerned, and  $IC_{r,i}$  = the IPR holder's incremental costs of remaining inputs)<sup>158</sup>

It is easy to observe from the equation (1) that, if the incremental costs of other inputs remain the same, the implicit royalty rate the IPR holder charges itself for using the IPR varies by the amount that the price of the final product varies. This equation applies also in the cases where the requested IPR serves as an essential input for different final products and their final prices are different. As Swanson and Baumol put it, "*any discrimination in the IP owner's final product prices must be mirrored precisely in its IP license fees*".<sup>159</sup> This equation is considered to be also capable of calculating the implicit price a firm holding other bottleneck inputs charges itself for using such input which is essential for the production of the downstream market.<sup>160</sup> It could be observed that the equation (1) is not capable of – and it is not designed for – eliminating or reducing any monopoly profit.<sup>161</sup> Excessive pricing, which originates from insufficient competition in the upstream IP market, could not be eliminated in the absence of a limitation on the price of the final product.<sup>162</sup> Swanson and Baumol consider that this so-called 'deficiency' of the ECPR only passes the undesirable price of the final product onto the royalty rate setting.<sup>163</sup>

The equation (1) should be equivalent to another equation (2) as demonstrated below:

$$(2) P_i = IC_i + \text{the IPR holder's incremental opportunity cost of licensing to others} = IC_i + \text{the IPR holder's profit per unit of downstream product.}$$

(Where  $IC_i$  = any direct incremental cost per unit of downstream product the IPR holder

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<sup>157</sup> Ibid.

<sup>158</sup> Ibid, pp.30-32.

<sup>159</sup> Ibid, p35.

<sup>160</sup> Ibid, pp.30-31.

<sup>161</sup> Ibid, pp.42-44.

<sup>162</sup> Ibid.

<sup>163</sup> Ibid, pp.42-43.

incurs to use the IPR itself or to license it to others) <sup>164</sup>

As shown above, in order to meet the ‘non-discriminatory’ requirement, the implicit royalty rate the IPR holder charges itself should be the IPR holder’s incremental costs incurred in IPR licensing, plus its incremental opportunity cost. The latter should, under such assumption, be interpreted as the IPR holder’s lost profit which has been taken away by the licensees.<sup>165</sup>

The equivalence between the equation (1) and the equation (2) bases its premise on the assumption that the final products provided by the IPR holder and those by its rivals are perfect substitutes on the downstream market. However, such equivalence would not be established if the final downstream products offered by the rivals are not perfect substitutes for the IPR holder’s product.<sup>166</sup> In such cases where the sales expansion of the rival’s final product could merely take away one portion (rather than the whole) of the IPR holder’s sales of its final product, the IPR holder’s incremental opportunity costs of licensing to others in the equation (2), namely its profit lost due to the licensing, would be correspondingly lower than that in the perfect substitution assumption. It is therefore apparent that, if everything else stays equal, the implicit royalty rate calculated by the equation (1) would be higher than that obtained from the equation (2). In such cases, the result of the equation (2) would be more appropriate.

The ‘reasonable’ royalty rate obtained from the *ex ante* auction-like process – the first part of this economic model, and the ‘non-discriminatory’ royalty rate determined from the ECPR principle – the second part of this model, according to Swanson and Baumol’s analysis, should generally be the same, either in the case where an IPR holder facing little competition, or in the case where the IPR licensing market is highly competitive.<sup>167</sup> Too low or too high royalty rates would not be accepted by the equally efficient licensees in the downstream market if “downstream barriers to entry are low *regardless of competitive conditions in the technology licensing market*”.<sup>168</sup>

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<sup>164</sup> Ibid, p32.

<sup>165</sup> Ibid.

<sup>166</sup> The following analysis about application of ECPR in imperfect substitution situation is based on Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.44-45.

<sup>167</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.37-40.

<sup>168</sup> Ibid, p39.

### 3.3.3 The Epstein-Marcus Model

Another economic framework – Financial Indicative Running Royalty Model (‘FIRRM’) is proposed by Epstein and Marcus, aiming at reducing the uncertainty deriving from the *Georgia-Pacific* approach<sup>169</sup> and realising more reliable results with less time and expense.<sup>170</sup> FIRRM compares the difference in profit between the best project choice incorporating the IPR at issue and the ‘next-best’ project choice (i.e. the downstream producer switches to adopt other alternative IPR or designs around the IPR at issue), thus determining a reasonable royalty rate from the perspective of investor’s profitability and cash flow.<sup>171</sup> Epstein and Marcus use economic concepts “net present value” (‘NPV’) and “internal rate of return” (‘IRR’) to set up this model. NPV is “the present value of the expected future cash flows, discounted at the cost of capital, net of the amount of any initial investment”, where the cost of capital is the rate required by the project investors to guarantee that they will not lose money as time goes by.<sup>172</sup> For example, assume that the up-front investment of certain project and cash flow in one year are respectively 100 euro and 121 euro, and the cost of capital is 10%. Then the future cash flow in this project will have a present value of 110 euro ( $\frac{121}{1+10\%} = 110$ ). The NPV in this case would be 10 euro, namely the result of the discounted value of future cash flow (110 euro) less the value of the up-front investment (100euro). The IRR is “the effective rate of interest rate earned on the investment, irrespective of the cost of capital”.<sup>173</sup> So in the example above, the IRR would be 21% ( $\frac{121-100}{100} = 21\%$ ), irrespective of the outside cost of capital 10% in that example. Subsequently Epstein and Marcus come to their first conclusion that a project is able to afford a royalty payment only when the IRR exceeds the cost of capital (the amount is called “IRR spread”).<sup>174</sup>

Following the fundamental rationale of FIRRM that a reasonable royalty rate could be determined by comparing the profit difference between the best choice incorporating the IPR at issue and the ‘next-best’ choice, Epstein and Marcus then consider that the maximum royalty rate would be equal to the difference in NPV between the best choice and the

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<sup>169</sup> See *supra* note 125.

<sup>170</sup> See Roy J. Epstein and Alan J. Marcus, ‘Economic analysis of the Reasonable Royalty: Simplification and Extension of the *Georgia-Pacific* Factors’ (2003) 85 *Journal of the Patent and Trademark Office Society* 555, p555.

<sup>171</sup> *Ibid*, p557.

<sup>172</sup> *Ibid*, pp.558-559.

<sup>173</sup> *Ibid*, p560.

<sup>174</sup> *Ibid*.

‘next-best’ choice.<sup>175</sup> For example, suppose that the best project in which the license of the IPR at issue is required need up-front investment of 100 euro and would generate cash flow of 121 euro after one year, with the cost of capital of 10%, the NPV of the best project would be 10 euro as explained in the previous paragraph. If the NPV of the ‘next-best’ project is 5 euro (which means, with the same cost of capital in the market, its potential cash flow after one year is 115.5 euro), the maximum chargeable royalty could be 5 euro (the best choice NPV 10 euro – the ‘next-best’ choice NPV 5 euro = 5 euro) if other elements in these two projects are equal.

Table 4: example of FIRRM

	Up-front investment	Cash flow in one year	Cost of capital	Present value	Net present value (NPV)
Best choice	100 euro	121 euro	10%	$121/(1+10\%)$ =110 euro	10 euro
Next-best choice	100 euro	115.5 euro	10%	$115.5/(1+10\%)$ = 105 euro	5 euro

Thus, the maximum reasonable royalty rate would make the potential licensee(s) indifferent between paying for access to the IPR at issue, and switching to the ‘next-best’ alternative.<sup>176</sup> A royalty rate below that maximum level would tempt the potential licensee(s) to pay for using the IPR at issue.

### 3.3.4 The feasibility of applying economic models in refusal to license cases

The Lemley-Shapiro model, the Swanson-Baumol model and the Epstein-Marcus model, from different economic perspectives, answer the question as to at which level a reasonable royalty rate (and a non-discriminatory royalty rate by the Swanson-Baumol model as well) should be set. As some observers comment, the approach to calculating the benchmark royalty rate in the Lemley-Shapiro model is “merely a starting point”, because “in the real world, knowing all three variables, or even reasonably approximating them may be impossible”.<sup>177</sup> Absent a perfectly transparent market where necessary information could be timely and sufficiently collected, the dominant undertaking that holds the essential IPR, even equipped

<sup>175</sup> Ibid, p560.

<sup>176</sup> Ibid, p562.

<sup>177</sup> Hal J. Singer and Kyle Smith, ‘What Does an Economist Have to Say About the Calculation of Reasonable Royalties’ (2009) 14(1) *Intellectual Property Law Bulletin* 7, p14.

with experienced economists, is not capable of quantifying each variable in a specific case. This difficulty could emerge in other two models as well. More importantly for the Lemley-Shapiro model which is invented mainly for IP infringement cases, it is not necessary and also not logical to take into account the IPR strength ( $\theta$ ) in the context of a follow-on refusal to license case like *Microsoft II*. If the strength of the IPR at issue is an open question in the refusal to license case, the IPR licensee, instead of complaining that such refusal has violated competition law, could have alleged that the IPR is invalid or his behaviour has not infringed the IPR. Therefore, the benchmark royalty rates should be equal to the negotiated royalty rate. The royalty rate setting should consider merely the bargaining power ( $B$ ) and the contribution of the IPR input to the final product ( $V$ ). Thus the reasonable royalty rate should amount to the result of  $B \times V$ .

As to the Swanson-Baumol model, a general comment is that a number of additional simplifications within the model would narrow the scope of its application in reality.<sup>178</sup> The main attraction of this model – the *ex ante* auction-like process to determine a reasonable royalty rate, is argued to be also its intrinsic limit on the grounds that negotiations for the royalty rates have not been recognized in this model as more relevant than such auctions.<sup>179</sup> The ‘reasonable’ royalty rate obtained from the *ex ante* auction-like process and the ‘non-discriminatory’ royalty rate determined from the ECPR principle, according to Swanson and Baumol’s analysis, should generally be the same. This may not be the case in a refusal to license situation. For different fields of use and different customers, reasonable royalty rates are not always uniform. On the contrary, it is unavoidable and not undesirable in a competitive market because the difference in production costs between the ‘best’ IPR and the ‘next-best’ IPR could vary among different producers on the downstream market.<sup>180</sup> Swanson and Baumol also admit that it is possible that, in conducting this auction-like process, an IPR holder could charge an excessive royalty rate as long as the information disclosed is incomplete, or in the situation where there are very limited competitors in the marketplace and the IPR holder dominates the market prior to the standard selection.<sup>181</sup> Therefore, the Swanson and Baumol’s *ex ante* auction seems merely appropriate in the cases where the IPR holder is competing with its rivals in a competitive market in the standard-setting context. It

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<sup>178</sup> See Mario Mariniello, ‘Fair, Reasonable and Non-Discriminatory (FRAND) Terms: A Challenge for Competition Authorities’ (2011) 7(3) *Journal of Competition Law and Economics* 523, working paper version, available at SSRN: <http://ssrn.com/abstract=2186052>, last visited on 18 November 2013, fn.11.

<sup>179</sup> Ibid, p5.

<sup>180</sup> See Daniel G. Swanson and William J. Baumol, ‘Reasonable and Nondiscriminatory (RAND) Royalties, Standards Selection, and Control of Market Power’ (2005) 73 *Antitrust Law Journal* 1, pp.23-24.

<sup>181</sup> Ibid, p21 and p23.

may not be suitable for the cases, such as the typical refusal to license cases, where the IPR holder faces no effective competitor in the relevant market.

As regards the ECPR principle, some commentators contended that one notable deficiency is that, once the IPR holder is not vertically integrated and thus does not provide final product incorporating the IPR concerned on the downstream market, it would be difficult to discover the implicit royalty rate the IPR holder charges itself.<sup>182</sup> This occurs however rarely in the refusal to license scenario, since the dominant undertaking generally has incentive to refuse to license other undertakings on the downstream market to use its IPR only when the IPR holder also provides his own product on that market.<sup>183</sup> The advantage of the set of ECPR equations lies in that all economic costs, including opportunity costs, have been taken into account when determining the non-discriminatory royalty rate.<sup>184</sup> But the refusal to license cases may have their special difficulties in applying ECPR. It should be reminded that the EU case law has established that prevention of the appearance of a new product on the downstream market is one fundamental requirement to establish an abusive refusal to license.<sup>185</sup> While it is not quite clear how much degree of innovation is required to make the downstream producer's product a 'new' product under Article 102 TFEU<sup>186</sup>, it would be somehow difficult to predict the IPR holder's opportunity costs (or the profit lost due to the new product's entry into the market) in order to determine the implicit royalty rate the IPR holder charges itself (the second ECPR equation calculates the implicit royalty rate as:  $P_i = IC_i + \text{the IPR holder's incremental opportunity cost of licensing to others} = IC_i + \text{the IPR holder's profit per unit of downstream product}$ ).

Lastly, concerning the applicability of the Epstein-Marcus model in refusal to license cases, it is obvious that this model bases its premise on the existence of the 'next-best' option other than incorporating the 'best' IPR into the final product for the downstream producers. That requires that either there is alternative IPR on the upstream market, or the downstream

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<sup>182</sup> See Hal J. Singer and Kyle Smith, 'What Does an Economist Have to Say About the Calculation of Reasonable Royalties' (2009) 14(1) *Intellectual Property Law Bulletin* 7, p16.

<sup>183</sup> *Commission Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings* [2009] OJ C 45/7, Para 76.

<sup>184</sup> See Hal J. Singer and Kyle Smith, 'What Does an Economist Have to Say About the Calculation of Reasonable Royalties' (2009) 14(1) *Intellectual Property Law Bulletin* 7, p16.

<sup>185</sup> See Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para 54; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para 49; Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 658.

<sup>186</sup> More analysis on the requirement of a new product could see chapter 3, section 2.3.

producer could invent around the IPR at issue. It appears, however, neither is available in a refusal case where the behavior has already been considered abusive. Otherwise, the ‘indispensability condition’ in the ‘exceptional circumstances test’ would not have been satisfied to find the refusal abusive. Apart from the non-existence of a ‘next-best’ option, approximating future cash flow of the licensee’s ‘new’ product could be a rather complex task for the IPR licensor.

## 4. Conclusion

The fact remains that neither the Court of Justice nor the EU Commission has formulated a predictable approach that allow the IPR holders to evaluate whether their royalty rates comply with the FRAND requirement. To strike a balance between maintaining competitive market order and providing sufficient compensation for IPR holders, economists have, from different angles, proposed several models, by which the economic value of the IPR at issue could be indirectly calculated and thus a FRAND royalty rate could be determined. However, even the economic discussion on FRAND royalties remains somewhat limited helpful since the “abstract and simplified” models leave many issues open in the real markets.<sup>187</sup> The limitation, as analyzed above, is particularly obvious in the licensing scenario following an abusive refusal to license ruling. As a result, some licensors tend to set their royalty rates “based on a ‘rule of thumb’ rather than rates based on quantitative metrics or analysis of profitability.”<sup>188</sup> On top of the royalty rates, there are additional important elements, monetary terms or non-monetary terms, to be negotiated in an IPR licensing in order to get the full commercial picture.<sup>189</sup> The real costs of a license must evaluate all the elements of the licensing terms, rather than merely rely on the assessment of the royalty rate.<sup>190</sup>

The *Huawei/IDC* case in the introduction of this chapter demonstrates that China is also pursuing excessive royalty rates in the IT industry. Then, it is important for the IPR holders, whose refusal to license has infringed Chinese competition law, to be informed beforehand, first of all, whether there is EU-like concept of FRAND within the Chinese competition legislations. Secondly, if the answer to the former question is affirmative, the IPR holders

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<sup>187</sup> See Mikko Valimäki, “A Flexible Approach to RAND Licensing”, (2008) 28(12) *European Competition Law Review* 686, p689.

<sup>188</sup> Lynda M. Applegate and Gavin Clarkson, ‘Intellectual Asset Valuation’, Harvard Business School, Case Study N9-801-192 (Harvard Business School Publishing, 2000), p4.

<sup>189</sup> See Damien Geradin, ‘Standardization and Technological Innovation: Some Reflections on Ex-ante Licensing, FRAND, and the Proper Means to Reward Innovators’ (2006) 29(4) *World Competition* 511, p519.

<sup>190</sup> Ibid.

should be aware of how (if any) the Chinese competition authority and the courts interpret the FRAND requirement and at which level a reasonable royalty rate should be set. The next chapter, in addition to the discussion of China's envisaged criteria on refusal to license itself, will investigate this follow-on issue as well, intending to discover whether China takes or is considering to take an EU-like position in this respect.



## CHAPTER V The Potential for China

### 1. Introduction

Prior to investigating the implications of EU's experience on refusal to license issue for China, it should be noticed that, since the economic reform from 1978, China has in general attached increasing importance to the protection of intellectual property rights ('IPR') by gradually establishing a relatively full-fledged legal system.<sup>1</sup> The transparency in judicial enforcement of IP laws has also been improved in recent years. The Chinese Supreme Court established an official website to publish court decisions in IPR cases, making it possible to access to most IPR decisions delivered by the Supreme Court at the central level, or other Chinese courts at the local level.<sup>2</sup> Since 2008, the Supreme Court has published its *Annual Report of Intellectual Property Cases*.<sup>3</sup> On top of that, since 2009 the Supreme Court has published its *Annual White Paper on Intellectual Property Protection by Chinese Courts* ('IP Protection White Paper').<sup>4</sup> Moreover, according to the decision of the third plenary session of the 18<sup>th</sup> Central Committee of the Communist Party of China which was held in 2013,<sup>5</sup> China will "strengthen the application and protection of intellectual property rights (IPR), improve the technological innovation incentive mechanism", and the possibility of setting up specialized IP courts is being taken into consideration.<sup>6</sup>

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<sup>1</sup> Chinese IPR laws include but are not limited to, *the Patent Law* (adopted in 1984, latest amended in 2008) and its implementing rules (adopted in 2001, latest amended in 2010), *the Copyright Law* (adopted in 1990, latest amended in 2010) and its implementing rules (adopted in 2002, latest amended in 2013), *the Trademark Law* (adopted in 1982, latest amended in 2013) and its implementing rules (adopted in 2002), *Regulation on Protection of New Varieties of Plants* (adopted in 1997, amended in 2013), *Regulation on Protection of Integrated Circuit Layout Design* (2001) and its implementing rules (2001), *Regulation on Computer Software Protection* (adopted in 2001, latest amended in 2013).

<sup>2</sup> See <http://ipr.court.gov.cn/>. According to IP Protection White Paper 2013, *infra* footnote 4, 61,368 judgments of IP cases delivered by all levels of Chinese courts have been accessible on that official site by the end of 2013.

<sup>3</sup> See <http://www.court.gov.cn/xwzx/yw/>.

<sup>4</sup> IP Protection White Paper 2009 – 2011 see <http://ipr.court.gov.cn/sfbhzhk/>, IP Protection White Paper 2012 see <http://www.chinacourt.org/article/detail/2013/04/id/949841.shtml>, IP Protection White Paper 2013 see <http://www.chinacourt.org/article/detail/2014/04/id/1283299.shtml>, last visited on 26 April 2014.

<sup>5</sup> *Decision of the Communist Party of China (CPC) Central Committee on Some Major Issues Concerning Comprehensively Deepening the Reform*, adopted in the third Plenary Session of the 18<sup>th</sup> CPC Central Committee in Beijing, 12 November 2013, available at [http://www.china.org.cn/chinese/2014-01/17/content\\_31226494.htm](http://www.china.org.cn/chinese/2014-01/17/content_31226494.htm), last visited on 1 April 2014.

<sup>6</sup> *Ibid*, point 13 "deepening reform of the management system for science and technology", Para 2.

Apart from the increasingly enhanced IPR protection<sup>7</sup>, recently more and more attention has been paid to distinguishing between legitimate exercise of IPR and abuse of IPR. In 2008 the State Council issued the *Outline of the National Intellectual Property Strategy*, in which the Chinese central government states that, with the purpose of *maintaining fair competition* in the market and protecting the public welfare, it will define the reasonable scope of intellectual property within relevant legislations to prevent abuses of intellectual property rights.<sup>8</sup> In this regard, the International Bar Association in its comments on one Anti-Monopoly Law draft<sup>9</sup> noted that:

“the borderline between fair exercise of IP rights and abuse of IP rights is not well defined under any jurisdiction. An attempt to draw a dividing line through legislation is commendable but should leave no illusions as to the urgent need for future clarification through case law or administrative practice. While it is difficult to expect prompt and comprehensive regulatory guidance on such a thorny issue, the scope and protection of intellectual property rights in the PRC economy are obviously very important matters for foreign investors and, we believe, significant Chinese market operators alike.”<sup>10</sup>

From the perspective of competition law, whether and which type of refusal to license IPR constitutes abuse of dominant market position should be addressed by competition law. However, the transitional stage, that China is currently in, and China’s market structures have limited the reach of the Anti-Monopoly Law (‘AML’).<sup>1112</sup> One report issued by the World Bank

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<sup>7</sup> On the (significant) improvements in the effectiveness of China’s IP enforcement, see for instance Yahong Li, ‘Pushing for Greater Protection: The Trend toward Greater Protection of Intellectual Property in the Chinese Software Industry and the Implications for Rule of Law in China’ (2002) 23(4) *University of Pennsylvania Journal of International Law* 637.

<sup>8</sup> The State Council of the People’s Republic of China, *Outline of the National Intellectual Property Strategy*, 5 June 2008, Para 14, available at [http://english.gov.cn/2008-06/21/content\\_1023471.htm](http://english.gov.cn/2008-06/21/content_1023471.htm), last visited on 31 March 2014.

<sup>9</sup> Working Group on the Development of Competition Law in the People’s Republic of China, International Bar Association, Comments on the Draft Anti-Monopoly Law of the People’s Republic of China (PRC), 23 August 2005, available at [http://www.ibanet.org/LPD/Antitrust\\_Trade\\_Law\\_Section/Antitrust/DevCompLaw\\_PRC.aspx](http://www.ibanet.org/LPD/Antitrust_Trade_Law_Section/Antitrust/DevCompLaw_PRC.aspx), last visited on 20 May 2014.

<sup>10</sup> Ibid, pp.69-70.

<sup>11</sup> See generally Wentong Zheng, ‘Transplanting Antitrust in China: Economic Transition, Market Structure, and State Control’, (2010) 32 *University of Pennsylvania Journal of International Law* 643.

<sup>12</sup> *Anti-monopoly Law of the People's Republic of China* (adopted at the 29th meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China on 30 August 2007 and effective since 1 August 2008, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=6351&lib=law&SearchKeyword=&SearchCKeyword=%B7%B4%C2%A2%B6%CF%B7%A8>, last visited on 29 January 2014).

along with the State Council<sup>13</sup> has observed that:

“More competition – domestic and international – will be the key to improving the efficiency and innovation capability of Chinese enterprises. To increase competition in domestic markets, further reforms will be needed to support private sector firms, such as lowering barriers to firm entry and exit, breaking up state monopolies or oligopolies in key industries (petroleum, chemicals, electricity distribution, and telecommunications), promoting the growth of dynamic SMEs and increasing their access to finance, stimulating much needed regional and local specialization, and encouraging spontaneous state enterprise reforms through competition.”<sup>14</sup>

With regard to the relationship between a well-established competition law system and the incentives for investments in innovative activities, the Organisation for Economic Co-operation and Development (‘OECD’) report<sup>15</sup> also states that:

“Product market competition is an important stimulus for innovation. In China, various market imperfections still distort competition: administrative interventions interfere with the normal functioning of markets, and improper or even illegal conduct as well as some degree of local protectionism hamper or distort competition. Market institutions also remain underdeveloped and inadequate. As a consequence innovative activity may not be adequately rewarded. The transition to more innovation-driven growth based on stronger intellectual property rights also requires a modern, properly enforced anti-trust law.”<sup>16</sup>

Borrowing foreign legal elements is more efficient for establishing a workable legal system, because the foreign experience is likely to increase the level of predictability in expecting how they could function in the new system.<sup>17</sup> Prior to the enactment of the AML, there was one universalist perspective from US experts that the US experience in antitrust law has produced a superior system and could be of much value and should thus be copied by other jurisdictions

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<sup>13</sup> The World Bank and the Development Center of the State Council of the People’s Republic of China, *China 2030, Building a Modern, Harmonious and Creative High-Income Society* (2012), available at <http://www.worldbank.org/content/dam/Worldbank/document/China-2030-complete.pdf>, last visited on 14 April 2014.

<sup>14</sup> Ibid, p27.

<sup>15</sup> Organisation for Economic Co-operation and Development, *OECD Reviews of Innovation Policy: China* (OECD Publishing, 2008), available at [http://www.keepeek.com/Digital-Asset-Management/oecd/science-and-technology/oecd-reviews-of-innovation-policy-china-2008\\_9789264039827-en#page1](http://www.keepeek.com/Digital-Asset-Management/oecd/science-and-technology/oecd-reviews-of-innovation-policy-china-2008_9789264039827-en#page1), last visited on 2 January 2014.

<sup>16</sup> Ibid, p41.

<sup>17</sup> See e.g. David J. Gerber, ‘Constructing Competition Law in China: The Potential Value of European and U.S. Experience’ (2004) 3 *Washington University Global Studies Law Review* 315, pp.315-316.

including China.<sup>18</sup> The circumstances surrounding the creation, and the evolution of the US antitrust system, which heavily rely on the courts and judges, have limited relevance for the Chinese situation.<sup>19</sup> Rather, as elaborated in Chapter 1, the similar problems that China currently face and the EU has faced, and to some extent the similar legal traditions shared by China and the EU, make the EU experience in particular valuable for Chinese policy makers.<sup>20</sup> The *EU-China Competition Dialogue*<sup>21</sup> has established the EU competition law as the main reference model in China's own competition law development.<sup>22</sup> Apart from the AML, the development of secondary legislations, such as the NDRC's regulations targeting monopolistic pricing, has also demonstrated that EU competition law has become the main reference point for China's competition regulations.<sup>23</sup> In order to merge foreign legal elements into the entire system, it is fundamental to "re-contextualize them by examining how and why they were created, how they have developed, what their relationship is to other elements of the system, and what consequences they have produced".<sup>24</sup> Thus, the main questions to be answered in this chapter are, firstly whether the EU approaches on refusal to license IPR and the follow-on pricing issue are being considered by the Chinese lawmakers as the primary reference, and secondly how the EU approaches should be transplanted – in entirety or in part – to the Chinese legal and economic context. In addition to the substantial competition rules relating to refusal to license practice and follow-on pricing issue, a more efficient and integrated competition law enforcement regime is also inevitable for the enforcement of AML rules in technologically complex competition cases (for instance those at the IP-Antitrust interface). Thus, this thesis also includes an institutional reform proposal in the final section of this chapter.

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<sup>18</sup> See generally Jacques de Lisle, 'Lex Americana?: United States Legal Assistance, American Legal Models, and Legal Changes in the Post-Communist World and Beyond', (1999) 20(2) *University of Pennsylvania Journal of International Economic Law* 179.

<sup>19</sup> See David J. Gerber, 'Constructing Competition Law in China: The Potential Value of European and U.S. Experience' (2004) 3 *Washington University Global Studies Law Review* 315, pp.320-321.

<sup>20</sup> Ibid, p325.

<sup>21</sup> See chapter 1, section 4.

<sup>22</sup> See Qianlan Wu, 'EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law' (2012) 18(3) *European Law Journal* 461, pp.465-473.

<sup>23</sup> See generally Qianlan Wu, 'EU – China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law' (2012) 18(3) *European Law Journal* 461.

<sup>24</sup> David J. Gerber, 'Constructing Competition Law in China: The Potential Value of European and U.S. Experience' (2004) 3 *Washington University Global Studies Law Review* 315, p316.

## 2. The Competition-IPR intersection provisions within current Chinese laws

### 2.1 Provisions within Chinese laws other than the AML

Prior to the enactment of the AML, some Chinese laws and regulations have already tackled the intersection of competition and IP protection, focusing mainly on the IP protected technology licensing scenario. The *Chinese Contract Law* (1999)<sup>25</sup> provides that “[a] technology contract which illegally monopolizes technology, impairs technological advancement or infringes on the technology of a third party is invalid”.<sup>26</sup> Another article of the *Contract Law* stipulates that the licensor and the licensee may negotiate the scope of patent implementation and how the licensee may use the technical secrets, “provided that it may not restrict technological competition and technological development.”<sup>27</sup> These general principles then have been elaborated upon in subsidiary legislations, such as *Regulations on Administration of Import and Export Technologies* (2001)<sup>28</sup> and *Regulations for the Implementation of the Law on Chinese-Foreign Joint Ventures* (2001)<sup>29</sup>. In 2004 the Supreme Court issued a *Judicial*

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<sup>25</sup> *Contract Law of the People’s Republic of China*, adopted and came into force in 1999, translation available by subscription at <http://lawinfochina.com/display.aspx?id=6145&lib=law&SearchKeyword=&SearchCKeyword=%ba%cf%cd%ac%b7%a8>, last visited on 5 April 2014.

<sup>26</sup> *Ibid*, Article 329.

<sup>27</sup> *Ibid*, Article 343.

<sup>28</sup> *Regulations of the People’s Republic of China on Administration of Import and Export of Technologies*, adopted in 2001 and revised in 2011, translation available by subscription at <http://lawinfochina.com/display.aspx?id=2251&lib=law&SearchKeyword=&SearchCKeyword=%bc%bc%ca%f5%bd%f8%b3%f6%bf%da>, last visited on 5 April 2014. (Article 29: “The following restrictive clauses shall not be included in a contract of import of technologies: (1) Clauses requiring the assignee or licensee to accept such conditions which are not indispensable for the import of the technologies as purchasing unnecessary technologies, raw materials, products, equipment or services; (2) Clauses requiring the assignee or licensee to pay fees or assume certain obligations for using technologies the patented period of which has expired and the patent of which has been declared as void; (3) Clauses restricting the assignee or licensee to make improvement on the technologies or to use such improved technologies; (4) Clauses restricting the assignee or licensee to obtain from sources other than the assignor or licensor technologies similar to or competitive with those provided by the assignor or licensor; (5) Clauses unreasonably restricting the channels or sources for the assignee or licensee to purchase raw materials, spare parts, products or equipment; (6) Clauses unreasonably restricting the quantity, type and price of the products of the assignee or licensee; (7) Clauses unreasonably restricting the export of the products produced by the assignee or licensee by using the imported technologies.”)

<sup>29</sup> *Regulations for the Implementation of the Law of the People’s Republic of China on Chinese-Foreign Joint Ventures*, adopted in 1983 and amended in 1986, 1987 and 2001, translation available by subscription at <http://lawinfochina.com/display.aspx?id=2011&lib=law&SearchKeyword=&SearchCKeyword=%d6%d0%cd%e2%ba%cf%d7%ca%be%ad%d3%aa%c6%f3%d2%b5%b7%a8>, last visited on 5 April 2014. (Article 43: “The technology transfer agreements signed by a joint venture shall be submitted for approval to the examination and

*Interpretation on Disputes over Technology Contracts*<sup>30</sup>, in which the Supreme Court interpreted Article 329 of the *Contract Law*, and held that the following clauses would illegally monopolize technology and impair technological development in the market and thus should be void:

“(1) Restricting one party from making new research and development on the basis of the contractual subject technology, or restricting this party from using the improved technology, or the conditions for both parties to exchange the improved technologies with each other being not reciprocal, including such circumstances as requiring one party to gratuitously provide the other party with the improved technology, to transfer the improved technology to the other party non-reciprocally, to gratuitously and solely occupy, or jointly own the intellectual property of the improved technology; (2) Restricting one party from obtaining, from other origins, the technology similar to or competitive against that of the technology provider; (3) Impeding one party's sufficient exploitation of the contractual subject technology in a reasonable way pursuant to the market demands, including unreasonably restricting the quantity, varieties, price, sales channel or export market of the contractual subject technology exploited by technology acceptor in an obvious way to produce products or to provide services; (4) Requiring the technology acceptor to accept attached conditions dispensable for exploiting the technology, including purchasing dispensable technologies, raw materials, products, equipment, services or accepting dispensable persons, etc.; (5) Unreasonably restricting the channels or origins for the technology acceptor to purchase raw materials, parts and components, products or equipment, etc.; and (6) Prohibiting the technology acceptor from making objections to the effectiveness of the intellectual property of the contractual subject technology, or attaching conditions to the objections made.”<sup>31</sup>

Besides these rules within contract law system mostly imposing restrictions on IP licensing, one should note that in the IP law system the competition-IPR intersection has also been tackled

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approval authority. Technology transfer agreements shall comply with the following stipulations: (1) Expenses for the use of technology shall be fair and reasonable. (2) Unless otherwise agreed upon by both parties, the technology exporting party shall not put any restrictions on the quantity, price or region of sale of the products that are to be exported by the technology importing party. [...] (7) No irrational restrictive clauses prohibited by Chinese law and regulations shall be included.”)

<sup>30</sup> Interpretation of the Supreme People's Court concerning Some Issues on Application of Law for the Trial of Cases on Disputes over Technology Contracts, adopted in 2004 and came into force in 2005, translation available by subscription at <http://lawinfochina.com/display.aspx?id=3910&lib=law&SearchKeyword=&SearchCKeyword=%b9%d8%d3%da%c9%f3%c0%ed%bc%bc%ca%f5%ba%cf%cd%ac%be%c0%b7%d7>, last visited on 5 April 2014.

<sup>31</sup> Ibid, point 10.

in the patent compulsory license provision in the *Chinese Patent Law*.<sup>32</sup> Article 48 of the *Patent Law* provides that, the national patent administrative authority may, upon the application of an eligible entity or individual, issue a compulsory license order against the patent holder, if the patentee's exercise of his rights constitutes a "monopolizing act" and the compulsory license granted would eliminate or reduce the anti-competitive effects caused by such conduct.<sup>33</sup> Yet, due to the nature and scope of IP law, this provision does not, and should not be expected to address the concern as to which behaviour, or specifically whether unilateral and unconditional refusal to license IPR would constitute a monopolizing act.

## 2.2 Provision within the AML

Under the competition law frameworks of other jurisdictions, there are generally two approaches to defining the relationship between the exercise of IPR and the enforcement of competition rules.<sup>34</sup> Either, as in the EU and the US, the general competition laws do not specify whether the competition rules shall apply to the exercise of IPRs, but such provisions are included in regulations or enforcement guidelines.<sup>35</sup> Another approach is adopted by some other jurisdictions such as Japan where the general competition law explicitly states the principle that the competition law shall not apply to the legitimate exercise of IPRs<sup>36</sup>, and specific regulations or guidelines provide which behaviour constitute abuse of IPR and consequently would not be exempted from the application of competition law.<sup>37</sup> The final

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<sup>32</sup> *Patent Law of the People's Republic of China*, adopted on 12 March 1984, amended in 1992, 2000 and 2008, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7289&lib=law&SearchKeyword=&SearchCKeyword=%d7%a8%c0%fb%b7%a8>, last visited on 7 March 2014.

<sup>33</sup> Ibid, article 48, Para 2.

<sup>34</sup> See Zhenguo Wu, 'Perspectives on the Chinese Anti-Monopoly Law' (2008) 75 *Antitrust Law Journal* 73, p96.

<sup>35</sup> E.g. *Commission Regulation (EU) No 316/2014 of 21 March 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements*, [2014] OJ L 93/17; *Communication from the Commission Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements* [2014] OJ C 89/3; US Department of Justice and Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property* (1995); US Department of Justice and Federal Trade Commission, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (2007).

<sup>36</sup> For example, in Japan see *Act on Prohibition of Private Monopolization and Maintenance of Fair Trade* (Act No.54 of 14 April 1947), available at [http://www.jftc.go.jp/en/legislation\\_gls/amended\\_ama09/index.html](http://www.jftc.go.jp/en/legislation_gls/amended_ama09/index.html), last visited on 15 December 2013, Article 21.

<sup>37</sup> For example, in Japan see *Guidelines for the Use of Intellectual Property under the Antimonopoly Act* (2007), available at [http://www.jftc.go.jp/en/legislation\\_gls/imonopoly\\_guidelines.files/070928\\_IP\\_Guideline.pdf](http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/070928_IP_Guideline.pdf); *Guidelines on Standardization and Patent Pool Arrangements* (2005), available at [http://www.jftc.go.jp/en/legislation\\_gls/imonopoly\\_guidelines.files/Patent\\_Pool.pdf](http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/Patent_Pool.pdf), last visited on 15 December

text of the AML (and the corresponding article in the previous drafts, as will be elaborated below) has adopted the latter approach, stating in its Article 55 that

“[t]his law shall not apply to the conduct of business operators exploiting their intellectual property rights in accordance with intellectual property laws and relevant administrative regulations; however, this Law shall apply to the conduct of business operators with the effect of eliminating or restricting market competition by abusing their intellectual property rights.”<sup>38</sup>

### **2.2.1 Article 55 and its predecessors**

It is claimed that Article 55 of the AML as well as its corresponding articles in previous drafts, which address the applicability of competition rules to abuse of IPRs, might be the most controversial provision in the AML, because for one thing the article itself is rather vague, for another the status of IP protection in China is also a controversial issue.<sup>39</sup>

In one previous AML draft prepared in 2002 (‘2002 Draft’), Article 56 of that draft provided as follows:

“[t]his law is not applicable to the conduct of business operators exploiting intellectual property in accordance with the copyright law, trademark law and other laws protecting intellectual property rights. However, this law shall apply where there is abuse of intellectual property rights with the effect or potential effect of over-broadly limiting or eliminating competition.”<sup>40</sup>

As an active commentator, American Bar Association (‘ABA’)<sup>41</sup> in 2003 submitted its comments on the 2002 Draft (‘2003 ABA comments’), expressing the U.S. competition law practitioners’ concern regarding the vagueness of this provision.<sup>42</sup> Since the 2002 Draft did not

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2013.

<sup>38</sup> AML, *supra* note 12, Article 55.

<sup>39</sup> See Mark S. Blodgett, Richard J. Hunter, Jr. and Robert M. Hayden, ‘Foreign Direct Investment, Trade, and China’s Competition Laws’ (2009) 37(2) *Denver Journal of International Law and Policy* 201, p224.

<sup>40</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, footnote 9. The 2002 Draft was prepared by the former State Economic and Trade Commission (this Commission was abolished in a government restructuring in 2003 and its place as the main drafter has been taken by the MOFCOM since then) and the full text was unpublished.

<sup>41</sup> It should be noticed that, beside ABA, there were other entities from other jurisdictions invited by related Chinese authorities to comment on the 2002 draft AML and the later 2005 draft AML. However, ABA’s comments in 2003 and 2005 are the only publicly available documents, which could be accessed as indicated in *infra* notes 42 and 46.

<sup>42</sup> Joint Submission of the American Bar Association’s Sections of Antitrust Law and International Law and Practice



provide any guidance as to what constitutes ‘abuse of intellectual property rights’, they feared that mere exercise of IPR, such as IPR holder’s unconditional refusal to license other enterprises the right to access to its IPR, may be treated as an abuse by this provision.<sup>43</sup> It would result in such an unintended consequence that IP protection imposed by relevant IP laws would be removed. To avoid such adverse impact on innovation, 2003 ABA comments suggested that the provision should be revised in a manner that at least the unilateral exercise of IPR “to exclude, inherent in the ownership of intellectual property, shall not constitute an abuse”.<sup>44</sup>

Later in another AML draft prepared in 2005 (‘2005 Draft’), Article 56 of that draft provided as follows:

“[t]his law is not applicable to undertakings who exercise their rights under the Patent Law, the Trademark Law and the Copyright Law. However, abuse of intellectual property rights in violation of this Law will be dealt with pursuant to this Law.”<sup>45</sup>

In ABA’s comments submitted in May 2005 (‘2005 ABA comments’), U.S. practitioners firstly raised doubt on the removal of the language “other laws protection intellectual property rights” from the 2002 Draft and argued that such deletion would nullify IP protection conferred by other relevant laws.<sup>46</sup> Then, 2005 ABA comments repeated its concern on the continued absence of any definition of ‘abuse of intellectual property rights’, and reiterated that without further guidance this provision would increase the likelihood that an unconditional and

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on the Proposed Anti-Monopoly Law of the People’s Republic of China (July 15, 2003), in supplementation of the Joint Submission of the American Bar Association’s Sections of Antitrust Law, Intellectual Property Law and International Law on the Proposed Anti-Monopoly Law of the People Republic of China (May 19, 2005), available at

[http://www.americanbar.org/content/dam/aba/administrative/antitrust\\_law/comments\\_prc2005wapp.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_prc2005wapp.authcheckdam.pdf), last visited on 20 May 2014, p31.

<sup>43</sup> Ibid.

<sup>44</sup> Ibid.

<sup>45</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, footnote 9. The State Council in April 2005 released the 2005 draft Anti-Monopoly Law for comments, the full text of which is however not accessible online now.

<sup>46</sup> Joint Submission of the American Bar Association’s Sections of Antitrust Law, Intellectual Property Law and International Law on the Proposed Anti-Monopoly Law of the People Republic of China (May 19, 2005), available at [http://www.americanbar.org/content/dam/aba/administrative/antitrust\\_law/comments\\_prc2005wapp.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_prc2005wapp.authcheckdam.pdf), last visited on 20 May 2014, p34.

unilateral refusal to license may be regarded as an abuse.<sup>47</sup> Like the 2002 ABA comments, ABA advocated that at least the unilateral exercise of IPR “to exclude, inherent in the ownership of intellectual property, shall not constitute an abuse”.<sup>48</sup> Afterwards, ABA in its supplementation of the 2005 ABA comments additionally proposed that:

“the term ‘abuse’ should be defined to ensure that a mere unilateral refusal to license, without any ancillary anticompetitive conduct and without any purpose or effect of creating or maintaining market power not otherwise granted by the IP in question, would not be found to constitute a violation of the Anti-Monopoly Act.”<sup>49</sup>

Likewise, concerning the IPR provision in the 2005 Draft, the working group of the International Bar Association also attached importance to a timely guidance on the concept of abuse of intellectual property rights, “especially as intellectual property laws are typically silent on competition-related questions.”<sup>50</sup>

The final approved IPR provision (Article 55) in the AML however does not incorporate the international practitioners’ suggestions. Rather than an enforceable competition law rule, Article 55 is merely a statement, leaving adequate space for follow-on guidance on IPR-related competition issues and also leaving *a number of questions* to be answered. In fact, the first half of the Article 55 is of little importance, since legitimate exercise of intellectual property rights protected by IP laws should not be the subject of competition law as long as the rights have not been unduly exploited by the owner. As to the second half of Article 55, like its predecessors it is still vague what conduct constitutes an abuse of IPR with anti-competitive effects. In October 2007 the EU during a WTO Council for TRIPs meeting raised a question as to whether China could clarify the meaning of ‘abuse of intellectual property rights’ in practice.<sup>51</sup> The ambiguity of the Article 55 of the AML has also raised

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<sup>47</sup> Ibid.

<sup>48</sup> Ibid.

<sup>49</sup> Proposed Revisions to Selected Articles of The April 8, 2005 Revised Draft of The anti-Monopoly Law of the People’s Republic of China, In Supplementation of the Joint Submission of the American Bar Association’s Sections of Antitrust Law, Intellectual Property Law and International Law, On the Proposed Law, dated 19 May, 2005, available at [http://docs.law.gwu.edu/facweb/dclarke/chinalaw/features/documents/ABA\\_July05Comments-PRC\\_AML.pdf](http://docs.law.gwu.edu/facweb/dclarke/chinalaw/features/documents/ABA_July05Comments-PRC_AML.pdf), last visited on 20 May 2014, p27.

<sup>50</sup> Working Group on the Development of Competition Law in the People’s Republic of China, International Bar Association, Comments on the Draft Anti-Monopoly Law of the People’s Republic of China (PRC), 23 August 2005, available at [http://www.ibanet.org/LPD/Antitrust\\_Trade\\_Law\\_Section/Antitrust/DevCompLaw\\_PRC.aspx](http://www.ibanet.org/LPD/Antitrust_Trade_Law_Section/Antitrust/DevCompLaw_PRC.aspx), last visited on 20 May 2014, p70.

<sup>51</sup> See paragraph 23 of the Communication from the European Communities under the transitional review

concern from the US antitrust law experts that this article would empower the competition law enforcement authorities and Chinese courts to take a similar stance with that of US antitrust policy between 1930s and the mid-1970s, by adopting measures, *inter alia* imposing compulsory licensing obligation, to weaken multinational enterprises' legitimate IPRs.<sup>52</sup> And one should note that the change in US antitrust policy with respect to IPR, from the hostility toward IPR to the extensive use of the rule of reason in IPR cases, has been recognized as one cause for the growth and success of US companies in the technology-intensive industries.<sup>53</sup> However, it is believed that, due to local favouritism, it would be difficult for multinational companies to vindicate IPRs in China when their conducts have been judged as having caused anti-competitive effects according to Chinese standards which might be largely different from those of the EU and the US.<sup>54</sup> IPR holders acutely concerned that the stakes are potentially very large, since unconditional, unilateral refusal to license IPR, which is normally regarded as a basic right of the right holder, may be treated as abusive behaviour if the Chinese enforcement authorities presume that IPR confers market power.<sup>55</sup> Some commentators are optimistic that this provision will be clarified and sufficient protection for IPR holders will be offered, but more observers are not so positive.<sup>56</sup> This is the *first question* to be answered by

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mechanism of China, IP/C/W/503, 11 October 2007, available at [http://trade.ec.europa.eu/doclib/docs/2008/september/tradoc\\_140343.pdf](http://trade.ec.europa.eu/doclib/docs/2008/september/tradoc_140343.pdf), last visited on 26 March 2014.

<sup>52</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, pp.75-78.

<sup>53</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, pp.77-82.

<sup>54</sup> See R. Hewitt Pate, 'What I heard in the Great Hall of the People – Realistic Expectations of Chinese Antitrust' (2008) 75 *Antitrust Law Journal* 195, pp.206-207; Yin Zhou, 'China's Anti-Monopoly Law: Insights from U.S. and EU Precedents on Abuse of Dominance and IP Exemption Provisions' (2009) 32(2) *Hastings International and Comparative Law Review* 711, p713.

<sup>55</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p153; Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p72. See also Gerald F. Masoudi, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, 'Some Comments on the Abuse-of-Dominance Provisions of China's Draft Antimonopoly Law', remarks presented to the UIBE Competition Law Center Conference on Abuse of Dominance: Theory and Practice, Beijing, China, 21 July 2007, available at <http://www.justice.gov/atr/public/speeches/225357.htm>, last visited on 24 December 2013.

<sup>56</sup> See Mark S. Blodgett, Richard J. Hunter, Jr. and Robert M. Hayden, 'Foreign Direct Investment, Trade, and China's Competition Laws' 2009 37(2) *Denver Journal of International Law and Policy* 201, pp.226-227. Interestingly, the national IP administrative authority in its National Patent Development Strategy (2011-2020) states that "[i]n accordance with relevant provisions of the Anti-monopoly Law, we will study and actively promote the development of standards and procedures to determine whether the abuse of patent right constitutes monopolistic behaviour." (the Notice of the State Intellectual Property Office on Issuing the National Patent Development Strategy (2011-2020), 26 October 2010, translation available by subscription at

the lawmakers.

Neither has Article 55 provided a clear meaning of ‘abuse of intellectual property rights’, nor has it clarified potential liability for violations of this Article.<sup>57</sup> It is unclear that once an abusive refusal to license IPR has been established, whether the enforcement authorities will issue a compulsory licensing order as a sanction, or the authorities will further determine the conditions of the compulsory licensing which might be unfair for the right holders.<sup>58</sup> Apart from an infringement finding, additional guidance regarding related remedies and follow-on issues appears thus to be necessary.<sup>59</sup> This is the *second question* to be answered by the lawmakers.

### 2.2.2 Refusal to license IPR and refusal to deal

Owing to the ambiguity of Article 55, the AML leaves the *third question* to be answered by the lawmakers whether the behaviour of refusal to license IPR will be treated in the same manner as refusal to supply other products. In other words, it should be clarified whether the standard in establishing an abusive refusal to deal under Article 17 of the AML is to be equally applied to refusal to license scenario.

Within AML’s ‘abuse of dominant position’ chapter, Article 17 specifies that undertakings holding a dominant position are prohibited from adopting some abusive conducts, in which one form of abusing dominant position is “refusing to deal with a trading partner without a valid justification”.<sup>60</sup> This requirement, for one thing, is inconsistent with the practice in both the US and the EU, where firms are free to choose business partners.<sup>61</sup> For another, Article 17 does not make it clear whether refusal to license IPR is subsumed as one form of refusal to deal, or otherwise IPR holder’s behaviour of refusal to license could be exempted from this prohibition. Some competition law specialists insist that in the absence of further guidance, other AML

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<http://www.lawinfochina.com/Display.aspx?Lib=law&Id=8611&keyword=>, last visited on 31 March 2014, emphasis added)

<sup>57</sup> See Mark S. Blodgett, Richard J. Hunter, Jr. and Robert M. Hayden, ‘Foreign Direct Investment, Trade, and China’s Competition Laws’ 2009 37(2) *Denver Journal of International Law and Policy* 201, p227; Yijun Tian, ‘The Impacts of the Chinese Anti-Monopoly law on IP Commercialization in China & General Strategies for Technology-driven Companies and Future Regulators’, (2010) 4 *Duke Law & Technology Review* 1, p10.

<sup>58</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p218.

<sup>59</sup> Ibid, pp.220-221.

<sup>60</sup> AML, *supra* note 12, Article 17.

<sup>61</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, p217.

provisions should be equally applied to the unilateral exercise of intellectual property rights, therefore refusal to deal prohibition in Article 17 could be extended to instances of refusal to license IPR.<sup>62</sup> The State Administration for Industry and Commerce (‘SAIC’) in its *AML implementing rules on the prohibition of abuse of dominant market position*<sup>63</sup> has enumerated five forms of prohibited refusal to deal, one of which is a dominant undertaking’s refusing the request from other undertakings for accessing to *essential facilities* under reasonable conditions without a valid justification.<sup>64</sup> However, it remains unclear whether essential IPR held by a dominant undertaking could be recognized as an *essential facility* for other undertakings to provide goods or services.<sup>65</sup> This is the key point in this *third question*.

Moreover, if refusal to license IPR is subsumed as one form of abusive refusal to deal prohibited by Article 17, the AML does not provide any guidance for the definition of ‘valid justification(s)’. The concept remains still vague even though the SAIC proposes in its AML implementing rules that for finding a valid justification in abuse of dominance cases, AML enforcement authorities should consider whether the dominant undertaking’s behaviour – including refusal to deal – is based on its normal commercial activities and for its normal benefits, and whether the behaviour has impact on the economic efficiency, public interests or economic development.<sup>66</sup>

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<sup>62</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, ‘China’s New Anti-Monopoly Law: A Perspective from the United States’ (2009) 18 *Pacific Rim Law & Policy Journal* 53, p75.

<sup>63</sup> *Provisions for the Industry and Commerce Administrations on the Prohibition of Abuse of Dominant Position* (adopted by the SAIC, issued on 31 December 2010 and effective since 1 February 2011, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8540&lib=law&SearchKeyword=Prohibition%20of%20Abuse%20of%20Dominant%20Market%20Position&SearchCKeyword=>, last visited on 20 January 2014).

<sup>64</sup> Ibid, Article 4. (“A business operator with a dominant market position is prohibited to refuse to deal with its counterparty in any of the following forms without justifiable reasons: 1. Reducing the current trading volume with the counterparty; 2. Deferring or terminating a current transaction with the counterparty; 3. Refusing to have new transactions with the counterparty; 4. Imposing restrictive conditions which makes it difficult for the counterparty to continue trading with the business operator; or 5. Refusing the counterparty’s request for using its necessary facilities under reasonable conditions in the course of production and operation. For finding a violation under Item (5), factors such as the following shall be considered comprehensively: feasibility in separately investing in and building or developing such facilities, degree of the counterparty’s reliance on such facilities for effective production and operation, possibility of the business operator making such facilities available, and its impact over the production and operation of the business operator.”)

<sup>65</sup> More discussion on ‘essential facility doctrine’ in the EU and the US, see chapter 2, section 3.1. In the *infra* sections 4.1.2 and 4.2.2 of this chapter, the Chinese version ‘essential facility doctrine’ formulated in the draft AML IP Guideline and the draft IP Enforcement Regulation will be analyzed.

<sup>66</sup> *Provisions for the Industry and Commerce Administrations on the Prohibition of Abuse of Dominant Position*,

### 3. Market definition and dominant position in IPR-intensive industries – case study of *Qihoo vs. Tencent*

Due to the ambiguous wording of Article 55, the previous sections have raised *three questions* to be answered by Chinese lawmakers in the competition-IPR intersection: the meaning of abuse of intellectual property rights (for this research precisely, the *first question* should be whether an unconditional, unilateral refusal to license IPR is abusive conduct), the liability of abuse of intellectual property rights (for this research, the *second question* concerns the liability of abusive refusal to license, and the follow-on issue of licensing fee setting), and the *third question* whether the lawmakers will adopt different standard in refusal to license IPR situations compared to that employed in other refusal to supply cases.

Apart from these concerns, the legal uncertainty of Article 55 has raised another *pre-question* as to whether this Article “may have extended the scope of the prohibition on abusing a dominant market position to activities that non-dominant companies carried out in an IP context”.<sup>67</sup> In other words, it is unknown whether the possession of a dominant position by the IPR holder in the relevant market is a precondition before the AML enforcement authority or the court advancing to assessing his allegedly abusive behaviour. If Article 55 is not interpreted broadly to apply the prohibition of the AML on abusing a dominant position to activities conducted by non-dominant companies, one scholar predicted that software companies otherwise may argue that they do not hold a dominant position due to the widespread piracy problem in China.<sup>68</sup> This also relates to the relevant market definition and market power assessment in IPR-intensive industries. In fact, prior to any AML guideline on IPR-related issues, Chinese courts have already demonstrated their understanding on whether the possession of a dominant position is a ‘must have’ precondition in the IP context in the ‘normal’ abuse of dominance cases (as well as the relevant market definition in IPR-intensive industries), *inter alia* by the recent significant civil competition law litigation between two Chinese software companies Qihoo and Tencent. Hereunder the case facts will be set out, followed by the comments.<sup>69</sup>

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*supra* note 63, Article 8.

<sup>67</sup> Yijun Tian, ‘The Impacts of the Chinese Anti-Monopoly law on IP Commercialization in China & General Strategies for Technology-driven Companies and Future Regulators’, (2010) 4 *Duke Law & Technology Review* 1, p10.

<sup>68</sup> *Ibid*, p14.

<sup>69</sup> More detailed analysis of this case could see Tiancheng Jiang, ‘The Qihoo/Tencent Dispute in the Instant Messaging Market: The First Milestone in the Chinese Competition Law Enforcement?’ (2014) 37(3) *World*

### 3.1 Case facts

*Qihoo/Tencent* is the most high-profile and complicated anti-monopoly lawsuit in the software industry before the Chinese courts since the enactment of the AML in 2008. Tencent, the defendant, is a Hong Kong-listed Chinese software company, whose popular instant messaging software product ('IM product') 'QQ' provides instant messaging service, with over 700 million active users by the end of 2011. Tencent also provides internet security software products, search engine, online media, gaming, interactive entertainment, e-commerce. Qihoo, the plaintiff, is a leading Chinese internet security software company, who offers a series of security software products including 'Qihoo 360 Safe Guard', with over 400 million active users by the end of 2011, and other software products such as '360 Anti-virus', '360 Internet Browser', '360 Safe for Mobile Handset' and related services. Tencent and Qihoo are the two biggest consumer software providers by the amount of active users in China. In September 2010, without any reminder to the users, Tencent upgraded its 'QQ Software Manager' and 'QQ Doctor' to 'QQ Computer Keeper', the main functions of which were almost the same as Qihoo's '360 Safe Guard'. Qihoo released its '360 Privacy Protector' which could be used to detect whether the users' privacy has been infringed by other software products such as QQ. In return, Tencent claimed that the 360 internet browser was engaged in promoting pornographic websites. On 27 October, Tencent and four other internet companies (Kingsoft, Baidu, Maxthon and Keniu) published a joint statement in order to boycott Qihoo. Two days later, Qihoo released its newly developed security tool '360 Koukou Guard', claiming that it could prevent QQ users' confidential files and private information from being monitored by QQ. On 3 November, Tencent published a letter to QQ users, requiring QQ users to un-install Qihoo's software if they wanted to continue using QQ. In other words, this letter obliged consumers to choose either Tencent's IM product QQ, or Qihoo's security software product. On 20 November, China's Ministry of Industry and Information Technology stepped into the feud between two companies and required them to restore interoperability for the sake of the software users.

In October 2011, Qihoo filed a lawsuit to the High Court of Guangdong Province ('the Guangdong Court') and claimed damages in the amount of RMB 150,000,000, alleging that Tencent<sup>70</sup> had abused its dominant position on the market for instant messaging software

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*Competition* 369.

<sup>70</sup> In fact, in this case Qihoo sued two companies as the defendants, both of which are within the Tencent group: the first defendant Tencent Technology (Shenzhen) Co., Ltd. – the software copyright holder, and the second defendant Tencent Computer System Co., Ltd. – the actual software controller, are joint operators of the IM product QQ. To be

products ('IM market') by firstly forcing its users to un-install Qihoo's security software and secondly abusively tying its security software with IM product QQ.<sup>71</sup> On 18 April 2012, the Guangdong Court held a public hearing that lasted for over seven hours.<sup>72</sup> On 28 March 2013, the Guangdong Court issued its judgment, finding that Qihoo wrongly defined the scope of relevant product and geographic market, and Tencent did not possess a dominant position in the IM market.<sup>73</sup> On 11 April 2013, Qihoo appealed to the Chinese Supreme Court against the first instance judgment of the Guangdong Court. The Supreme Court accepted the appeal and held a public hearing on 26 and 27 Nov 2013. On 16 October 2014 the Supreme Court delivered its final decision, which upheld the Guangdong Court judgment and most findings of the first instance court.<sup>74</sup>

## 3.2 The Guangdong Court judgment

### 3.2.1 Relevant product market

It is uncontested that in this case the relevant product is IM software and related services. The controversial issues are, firstly, whether the 'hypothetical monopolist SSNIP test' is appropriate to identify the scope of the relevant product market, and secondly, which products could be, by the software users, regarded as substitutes to the comprehensive IM products.

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clear, this paper will use 'Tencent' or 'the defendant' instead of 'Tencent Technology and Tencent Computer' and 'the defendants'.

<sup>71</sup> There are other two unfair competition litigations between Tencent and Qihoo. In October 2010, Tencent filed a complaint with the Chaoyang Court of Beijing against Qihoo. The Chaoyang Court of Beijing rendered its judgment in April 2011, ordering Qihoo to withdraw its '360 privacy protector' and to compensate Tencent in the amount of RMB 400,000. Full text of this judgment (in Chinese) is available at <http://cyqfy.chinacourt.org/public/paperview.php?id=549582>, last visited on 1 February 2014. In October 2011, after the abuse of dominance complaint filed by Qihoo, Tencent immediately sued Qihoo for unfair competition to the same court and claimed damages in the amount of RMB 120,000,000. The Guangdong Court rendered its judgment in favour of Tencent on 25 April 2013, ordering Qihoo to compensate Tencent in the amount of RMB 5,000,000, which was upheld by the Supreme Court in its final decision issued on 24 February 2014. Full text of the first instance judgment (in Chinese) is available at <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130425033621412641>, last visited on 1 February 2014.

<sup>72</sup> See news report at [http://news.xinhuanet.com/legal/2012-04/19/c\\_123005299.htm](http://news.xinhuanet.com/legal/2012-04/19/c_123005299.htm) (in Chinese), last visited on 1 February 2014.

<sup>73</sup> The full text of the judgment (in Chinese) could be accessed on the website of the Guangdong Court, <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130328040159946185>, last visited on 1 February 2014. ('the judgment of Guangdong Court').

<sup>74</sup> the full text of the final judgment (in Chinese) is available at [http://www.court.gov.cn/xwzx/yw/201410/t20141016\\_198470.htm](http://www.court.gov.cn/xwzx/yw/201410/t20141016_198470.htm), last visited on 27 October 2014. ('the final judgment')



Regarding the question of whether the SSNIP test is applicable in this case, Qihoo invoked an *Economic Analytical Report on the Antitrust Dispute between Qihoo and Tencent* provided by RBB economics LLP ('RBB Report'),<sup>75</sup> alleging that special attention should be paid to the unique pricing and profit mode of the IM market. According to Qihoo, it is a unique feature of the IM market that the basic services of the IM software are free of charge, and the IM software providers normally gain profits from the value-added services and advertisements. Apparently this business mode results in that price competition, especially for the basic services, does not even exist among the IM software providers. Therefore, according to Qihoo, the SSNIP test, which bases its quantitative analysis on an existing benchmark price, is not an appropriate approach in this case to determine the scope of the relevant product market.<sup>76</sup> The Guangdong Court admitted that many online products such as IM software, security software, search engine, email box, micro blog and Social Network Sites ('SNS'), are free for use on the internet for the consumers. The Guangdong Court maintained that consumers would switch to other free alternatives once the successful software provider started to charge for the basic services because consumers prefer undertaking the switching cost to sticking to the original software and paying for the basic services.<sup>77</sup> This conclusion could be drawn from the China Internet Network Information Centre's *China Instant Messaging User Research Report* ('CNNIC Report'), which concludes that up to 60.6 percent of IM software users in China would not continue using the same software if they have to pay for the basic services.<sup>78</sup> Surprisingly, the Guangdong Court, in order to support its viewpoint, for the first time quoted EU Commission's decision in *Microsoft/Skype* merger case<sup>79</sup>, in which the European competition regulator observed that more than 75 percent of Skype users "would cease using its free service if it started charging for it".<sup>80</sup> Therefore, the Guangdong Court still claimed to have employed the SSNIP test in defining the relevant product market.<sup>81</sup>

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<sup>75</sup> RBB's *Economic Analytical Report on the Antitrust Dispute between Qihoo and Tencent* was submitted as evidence by the plaintiff to the Court. Some conclusions of this economic analytical report have been quoted in the judgment, yet the full text could not be accessed online.

<sup>76</sup> The Judgment of Guangdong Court, *supra* note 259, Para 179.

<sup>77</sup> *Ibid.*

<sup>78</sup> China Internet Network Information Centre's *China Instant messaging User Research Report* (2009), available at <http://www.cnnic.net.cn/hlwfzyj/hlwzbg/201106/P020120709345301865898.pdf>, last visited on 1 February 2014, p29.

<sup>79</sup> COMP/M.6281 – Microsoft/Skype, Commission decision pursuant to Article 6(1) (b) of Council Regulation No 139/2004, 7 October 2011, full text is available at [http://ec.europa.eu/competition/mergers/cases/decisions/m6281\\_20111007\\_20310\\_2079398\\_EN.pdf](http://ec.europa.eu/competition/mergers/cases/decisions/m6281_20111007_20310_2079398_EN.pdf), last visited on 1 February 2014.

<sup>80</sup> *Ibid.*, Para 13, 76 and 121.

With regard to the interchangeable products within the IM market, Qihoo maintained that comprehensive IM software integrating instant text, voice and video communications, and related service, comprise the relevant product market.<sup>82</sup> Tencent, on the other hand, contended that the scope of relevant product market should be extended to include single-functioned IM software products, micro blog, SNS, and even telephone, fax, email.<sup>83</sup> First of all, the Guangdong Court drew an uncontested conclusion that the following three types of comprehensive IM software, as subdivided in the CNNIC Report<sup>84</sup>, belong to the same product market: general comprehensive IM software (e.g. QQ, MSN<sup>85</sup>), cross-platform comprehensive IM software (e.g. Fetion<sup>86</sup>) and cross-network comprehensive IM software (e.g. Skype).<sup>87</sup> Apart from the comprehensive IM products, there are other single-functioned IM products, such as text-only IM software, voice-only IM software and video-only IM software. The Guangdong Court considered that the functional distinction between comprehensive IM products and single-functioned IM products is, however, inadequate to prevent users from counting the latter as interchangeable products since consumers are sensitive to the potential price increase in the software market. Therefore the Guangdong Court concluded that each type of single-functioned IM products constitutes a part of a broader IM market rather than establishing a separate product market.<sup>88</sup> As to the telephone, fax and email services, the Guangdong Court quickly rejected Tencent's proposal to regard these as substitutes to IM software. The Guangdong Court considered these services could be clearly distinguished from IM products since the telephone and fax services are paid services while the basic services of the IM software are free<sup>89</sup>, and email is normally not used for *instant* communication which however is the main attraction of IM products<sup>90</sup>.

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<sup>81</sup> The Judgment of Guangdong Court, *supra* note 259, Para 179.

<sup>82</sup> *Ibid*, Para 98.

<sup>83</sup> *Ibid*, Para 103-113.

<sup>84</sup> China Internet Network Information Centre's *China Instant messaging User Research Report* (2009), available at <http://www.cnnic.net.cn/hlwfzyj/hlwzbg/201106/P020120709345301865898.pdf>, last visited on 29 October 2013, pp.8-9.

<sup>85</sup> The Microsoft has started to use Skype to replace its own product MSN (except in mainland China) after the Microsoft acquired Skype.

<sup>86</sup> Fetion is an IM software developed by China Mobile, a Chinese telecommunications company, allowing users to send and receive SMS between PC and mobile phone for free.

<sup>87</sup> The Judgment of Guangdong Court, *supra* note 259, Para 180.

<sup>88</sup> *Ibid*, Para 182.

<sup>89</sup> *Ibid*, Para 186.

<sup>90</sup> *Ibid*, Para 187.

The most controversial issue lies in whether micro blog and SNS should be identified as substitutes to the IM software. The Guangdong Court regarded micro blog and SNS as substitutes mainly on the grounds that, in the first place, micro blog and SNS could deliver almost the identical communication functions as the comprehensive IM software, i.e. sending and receiving messages instantly within consumers' personal social networks.<sup>91</sup> In this respect, the Guangdong Court quoted the reason put forward by the applicants in EU *Microsoft/Skype* case that, from the perspective of consumers, IM services "are increasingly used as an adjunct to other activities", and "a user experience which integrates a range of communication functionalities", such as Facebook and Google+, has been increasingly demanded.<sup>92</sup> In the second place, the Guangdong Court believed that comprehensive IM software users would switch to micro blog or SNS once the IM software providers started to charge for the basic services.<sup>93</sup> In the third place, the Guangdong Court added that internet industry, as analyzed in Chapter 2, is a fast moving industry where new technologies and business modes replace old ones quickly.<sup>94</sup> Therefore the future market development should also be taken into consideration. The fact that the *Qihoo/Tencent* dispute took place in the period when micro blog and SNS started to develop in China does not preclude the conclusion that it is possible to consider them as in the same product market with comprehensive IM products.<sup>95</sup>

### 3.2.2 Relevant geographic market

Regarding the relevant geographic market at issue, Qihoo argued that it should be confined to the mainland China due to the unique Chinese language and Chinese users' preference, while Tencent on the other hand claimed that geographically the IM market should be a global market.<sup>96</sup> The Guangdong Court ruled that mainland China as the relevant geographic market may be too narrow for the IM software. Above all, both of the providers and users of IM services are not confined to mainland China owing to the borderless feature of the Internet. On the one hand, overseas IM services providers have offered other alternatives, such as Skype and MSN, for the mainland China users. According to the judgment, Chinese language and consumers' preference do not act as market entry barrier to prevent overseas IM products from competing with Tencent's QQ in this case, since it is evident that nowadays overseas IM products could offer multilingual services, including Chinese, to cater to the consumers all

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<sup>91</sup> Ibid, Para 184.

<sup>92</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 25. The Judgment of Guangdong Court, *supra* note 259, Para 185.

<sup>93</sup> The Judgment of Guangdong Court, *supra* note 259, Para 185.

<sup>94</sup> See chapter 2, section 5.2.2.

<sup>95</sup> The Judgment of Guangdong Court, *supra* note 259, Para 185.

<sup>96</sup> Ibid, Para 191.

around the world. On the other hand, Tencent's QQ has also been used by some consumers in Hong Kong, Taiwan, Macao as well as other Chinese users living around the world. Furthermore, Tencent has provided non-Chinese versions of QQ for non-Chinese users. Lastly, the Guangdong Court found that, compared to other international trade of tangible products, there is no extra transportation or other related costs for the IM product providers as well as for the recipients.<sup>97</sup>

### 3.2.3 Establishing dominance

As long as the Guangdong Court found that both of the relevant product market and geographic market defined by Qihoo were too narrow, it comes as no surprise that the Court rejected the Qihoo's allegation that high market share of Tencent satisfies the dominance presumption provided in the AML.<sup>98</sup> The Guangdong Court firstly maintained that Tencent's market share calculated according to the relevant market, which was wrongly defined, could not reflect the genuine market power held by Tencent.<sup>99</sup> Secondly, the Court took one step back, concluding that the nature of the dynamically competitive industries determines that even if the relevant market was as narrow as Qihoo claimed, the dominance presumption based on Tencent's market share could also be rebutted on the grounds that Tencent had neither the ability to "control the price or quantity of commodities or other trading conditions in the relevant market", nor the ability to "block or affect the entry of other business operators into the relevant market".<sup>100</sup>

Regarding Tencent's market power compared to other existing competitors, according to the Guangdong Court the market leadership (within mainland China) did not attribute to Tencent absolute pricing power, since almost all the basic services of IM products are free of charge.<sup>101</sup> Also, it is apparent that Tencent would not unilaterally refuse to provide IM services to users or change other trading conditions for the reason that the software users could immediately switch to other interchangeable IM software available in the relevant market.<sup>102</sup> With respect to the question of whether the possession of a high market share in the relevant market would grant

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<sup>97</sup> Ibid.

<sup>98</sup> Article 19 of the AML, *supra* note 12, sets forth a series of rebuttable dominance presumptions, which provide that an undertaking will be presumed to hold a dominant position when he owns more than 1/2 of the total market share, or two undertakings jointly own more than 2/3 of the total market share, or three undertakings jointly own more than 3/4 of the total market share.

<sup>99</sup> The Judgment of Guangdong Court, *supra* note 259, Para 194.

<sup>100</sup> AML, *supra* note 12, Article 17(2).

<sup>101</sup> The Judgment of Guangdong Court, *supra* note 259, Para 197.

<sup>102</sup> Ibid.

Tencent the market power to block or affect the market entry of potential competitors, the Guangdong Court concluded that, even provided that Tencent held more than fifty percent market share in the IM market, competition on the merits from other IM service providers or the overall development of the IM market would not be impeded due to the following four reasons. In the first place, the IM market is a market with low barriers to entry for the potential competitors and it has been proved that the new entrants are possible to expand their business in a relatively short period.<sup>103</sup>

In the second place, while the Guangdong Court admitted the existence of network effect and consumer lock-in effect in the IM market, the judgment found that these effects were not capable of preventing QQ users from switching to other interchangeable products. Firstly, network effect in the IM market is not as strong as imagined since most users only use the instant communication services to contact, bilaterally, with their *core* relatives and friends, the amount of which is merely four to six according to the data from Facebook.<sup>104</sup> Secondly, similarly as what has been observed by the EU Commission in the *Microsoft/Skype* merger case, the Court considered that QQ was not a “must have” product.<sup>105</sup> It has been increasingly common that the consumers (could) have highly overlapped social networks on several IM platforms and they could thus freely and immediately switch to other alternatives.<sup>106</sup> Thirdly, the limitation of the consumer lock-in effect could also be indicated by the fact that the majority of Tencent’s market share was taken from its main ex-rival Microsoft’s MSN in a short period.<sup>107</sup>

In the third place, according to the Guangdong Court, any single market participant cannot control the market for a long period in a dynamically competitive industry where new technologies and new commercial modes emerge endlessly.<sup>108</sup> The competition among the traditional IM products has been further intensified as a result of the rise of the SNS and micro blog.<sup>109</sup>

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<sup>103</sup> Ibid, Para 199.

<sup>104</sup> Ibid, Para 200.

<sup>105</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 219.

<sup>106</sup> The Judgment of Guangdong Court, *supra* note 259, Para 200.

<sup>107</sup> Ibid.

<sup>108</sup> See chapter 2, section 5.2.2.

<sup>109</sup> The Judgment of Guangdong Court, *supra* note 259, Para 201.

In the fourth place, Tencent did not have such overwhelming advantages in technology and finance resource to prevent the existing competitors from expanding their market shares, or to prevent potential competitors from entering into the IM market.<sup>110</sup>

### 3.3 Comments

#### 3.3.1 IM market cases in the EU and China

In general, *Qihoo/Tencent* case is not only a significant private anti-monopoly lawsuit after the coming into force of the *AML judicial interpretation*.<sup>111</sup> More importantly, it might be the first milestone in the enforcement of the AML even taking into account the public enforcement cases.<sup>112</sup> This case has created a number of *firsts* in the history of AML enforcement. From the perspectives of the disputed parties, it is the *first* anti-monopoly case where both parties, in order to support their respective assertions, provided concrete evidences to the court, including several third parties' market research reports such as RBB Report, CNNIC Report and iResearch *China Instant Messaging Research Report (2009-2010)*<sup>113</sup>. In addition, it is the *first* anti-monopoly case where each party brought in expert witnesses to assist in clarifying the case facts, which is compliant with relevant provision in the AML judicial interpretation.<sup>114</sup> On the part of the courts, it is the *first* anti-monopoly case where Chinese courts analyzed substantial anti-monopoly issues, such as the scope of the relevant product and geographic market, the (non)existence of a market dominance position, in a quite detailed way (the length of the first instance judgment is 80 pages and the Supreme Court's final judgment is 115 pages), considering that traditionally Chinese judges do not write and publish long judgments

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<sup>110</sup> Ibid, Para 202.

<sup>111</sup> *Provisions of the Supreme People's Court on Several Issues concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct* (Interpretation No.5 [2012] of the Supreme People's Court, issued and came into force on 1 June 2012, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=9300&lib=law&SearchKeyword=Application%20of%20Law%20in%20the%20Trial%20of%20Civil%20Dispute%20Cases&SearchCKeyword=>, last visited on 1 February 2014, hereinafter 'AML judicial interpretation'). Supreme Court's judicial interpretations in practice are legally binding on the courts in China.

<sup>112</sup> There are numerous online comments describing *Qihoo/Tencent* case as the most significant antitrust case in China since the enactment of the AML, see e.g. <http://www.internationallawoffice.com/newsletters/detail.aspx?g=8cfe3e8e-2130-4a43-9bff-f5b153f985d7>; <http://media.people.com.cn/n/2013/0329/c40606-20957351.html>; [http://news.xinhuanet.com/legal/2013-04/16/c\\_124585565.htm](http://news.xinhuanet.com/legal/2013-04/16/c_124585565.htm), last visited on 1 February 2014.

<sup>113</sup> iResearch Consulting Group's *China Instant Messaging Research Report (2009-2010)*, available at <http://www.docin.com/p-91179870.html> (in Chinese), last visited on 1 February 2014.

<sup>114</sup> AML judicial interpretation, *supra* note 111, Article 12 provides that the parties may apply to the court for the appearance of one or two persons with professional knowledge to provide explanations in certain specialized areas in the court.

compared to their counterparts in the EU and the US.<sup>115</sup> Also, it is the *first* anti-monopoly case where a Chinese court claimed that it applied the SSNIP test in determining the proper scope of relevant product and geographic market. Regardless of whether the Guangdong Court rightly or wrongly adopted the SSNIP test in the IM market, this economic approach has rarely, or even never, been explicitly applied by either Chinese competition authorities or other Chinese courts in the enforcement of the AML.

More importantly, it is the *first* anti-monopoly case where some observations made by the EU Commission in an EU competition law case have been used by the parties to support their viewpoints, and then been confirmed and quoted by a Chinese court in its judgment. Since the Guangdong Court referred to some observations made by the EU Commission in *Microsoft/Skype* merger case,<sup>116</sup> discussion in this section would involve EU competition regulator's analysis in that case in defining the scope of the IM market and examining market power.<sup>117</sup> To begin with, it should be reminded that the criteria for defining the relevant market and the main question in examining the effect of certain behaviour on the competition between merger cases and dominance abuse cases are quite different, both in China and the EU. As to the scope of the relevant market concept, for one thing, merger cases and abuse of dominance cases are distinguished in the sense that, the price to take into account in a merger case will be the prevailing market price whereas in a dominance abuse case the fact that the prevailing price might already have been substantially increased should be taken into account.<sup>118</sup> For another, different scopes of the relevant market could result from the different time horizon considered since the examination of a merger case, where the analysis is essentially prospective, is different from the analysis of a past behaviour.<sup>119</sup> In addition, it is necessary to notice that the *Microsoft/Skype* merger review is a case where a definitive conclusion on the precise scope of

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<sup>115</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p242.

<sup>116</sup> The Judgment of Guangdong Court, *supra* note 259, Para 179, 185, 191 and 200.

<sup>117</sup> This section mainly analyzes the relevant market and market power in the IM market. Since the Guangdong Court ruled that Tencent did not possess a dominant position on the IM market, the Court – not obliged – but still responded to the question as to whether the allegedly abusive conducts had infringed the AML assuming Tencent held a dominant position on the IM market, which is however beyond the scope of the discussion in this section.

<sup>118</sup> See *Commission Notice on the definition of relevant market for the purposes of Community competition law*, (1997) OJ C 372/5, Para 19; *Guide of the Anti-Monopoly Committee of the State Council for the Definition of the Relevant Market* (issued and effective on 24 May 2009, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=7575&lib=law&SearchKeyword=Definition%20of%20the%20Relevant%20Market&SearchCKeyword=>, last visited on 1 February 2014, Article 11, Para 1.

<sup>119</sup> See *Commission Notice on the definition of relevant market for the purposes of Community competition law*, (1997) OJ C 372/5, Para 12.

the relevant market has not been reached because the transaction did not raise serious competition concern. With respect to the essence in analysing certain behaviour, competition authorities or courts investigate in merger cases whether a concentration would significantly impede effective competition in the market, and the creation or strengthening of a dominant position constitutes only one possible cause.<sup>120</sup> On the other hand, the essential question in evaluating an abusive conduct is whether a dominant position – possession of which is a precondition – has been unduly exercised.

However, based on the unique pricing and profit mode of IM products, *Qihoo/Tencent* case might be in such a particular position that the question as to whether the prevailing market price is competitive could be ignored. Furthermore, the dynamic competition nature of the IM market determines that a dominance abuse case should also be examined in a prospective way when defining the relevant market as well as assessing market power. Not only should the *status quo* be analyzed, but potential competitive constraints should also be taken into account.<sup>121</sup> Thus, the ‘time horizon’ concern in this case might not be as observable as in cases of other traditional industries. In addition, the factors related to market scope analysis and market power appraisal are, if not identical, similar between the *Microsoft/Skype* merger case and the *Qihoo/Tencent* case. Therefore, this thesis contends that these disparities do not necessarily lead to the conclusion that it is inappropriate to make a comparison between the analysis conducted by the EU Commission in *Microsoft/Skype* case and the Guangdong Court in *Qihoo/Tencent* case in determining the scope of the IM market and assessing market power.

### 3.3.2 Relevant product market: the SSNIP test and the IM market

The presiding judge in *Qihoo/Tencent* case claimed that the Guangdong Court innovatively applied the SSNIP test in defining the relevant market in the internet-based industry.<sup>122</sup> Before discussing the Guangdong Court’s view on the scope of relevant market, two preliminary questions have to be addressed: firstly, whether the Court *truly* applied the SSNIP test in its analysis, and secondly, whether the SSNIP test is applicable in the IM market. For the first doubt, throughout the ‘defining relevant market’ part of the judgment, the Court did not make extensive econometric and statistical analysis when examining whether other products (i.e. micro blog and SNS) are substitutes to comprehensive IM software products if a hypothetical

<sup>120</sup> Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings, OJ L24/1, Article 2, Para 3; AML, *supra* note 12, Article 28.

<sup>121</sup> See Tambiama Madiéga, ‘Innovation and Market Definition under the EU Regulatory Framework for Electronic Communications’ (2006) 29(1) *World Competition* 55, pp.57-66.

<sup>122</sup> See official Q & A of this case, available at <http://tech.sina.com.cn/i/2013-03-28/11288191110.shtml> (in Chinese, last visited on 1 February 2014).



small but non-transitory price increase was implemented. Rather, the Court relied on the products' characteristics and intended use to examine whether such products could serve as substitutes to which consumers of comprehensive IM software could switch. In other words, the Guangdong Court leaped directly from the assumption of a small but non-transitory price increase of the comprehensive IM software to its conclusion without conducting extensive econometric and statistical analysis in the middle. It seems the Court merely borrowed the concept of SSNIP but did not carry out the economic test. Moreover, doubt has been raised by some anti-monopoly law practitioners as to whether it is correct to apply the SSNIP test in the IM market where the unique pricing and profit mode determines there is no benchmark product price to start with.<sup>123</sup> The application of the SSNIP test by its definition requires that the relevant products provided are not free in order to implement a small but significant price increase of the candidate product (5% to 10%). Nevertheless, it is not possible to determine the hypothetical price if the relevant product at issue, IM software in this case, is free of charge. Placing a hypothetical price on the candidate IM products – even the added price is very low – would fundamentally convert the business mode of the market. The consequence is completely different with a hypothetical small but significant price increase on an originally charged product. The result of the survey would thus be unrealistic if the test has been implemented without considering the specific business mode of the IM market. The Supreme Court as expected ruled that the Guangdong Court inappropriately applied the SSNIP test.<sup>124</sup>

The EU Commission is not always willing to employ the SSNIP test since it requires “extensive econometric and statistical analysis”.<sup>125</sup> Instead, the Commission may rely on the following types of evidences to assess whether two products are demand substitutes: product characteristics and its intended use, evidence of substitution in the recent past, available quantitative evidence, views of customers and competitors, consumer preferences, barriers and costs associated with switching demand to potential substitutes, different categories of

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<sup>123</sup> A lot of Chinese anti-monopoly law practitioners have published their remarks on public sites or personal blogs. Most of them are against the application of SSNIP test in this case, i.e. Shilin Wei, available at [http://blog.sina.com.cn/s/blog\\_5a81db8501015ceq.html](http://blog.sina.com.cn/s/blog_5a81db8501015ceq.html); Hao Zhan, available at [http://www.anjielaw.com/publications\\_detail/newsId=f503106a-e728-4847-b70d-fc7d6ee69c5d.html](http://www.anjielaw.com/publications_detail/newsId=f503106a-e728-4847-b70d-fc7d6ee69c5d.html); Xu Liu, available at <http://www.antimonopolylaw.org/article/default.asp?id=4170>, last visited on 1 February 2014.

<sup>124</sup> The final judgment, *supra* note 74, pp. 80-81.

<sup>125</sup> Steven Anderman and Hedvig Schmidt, *EU Competition Law and Intellectual Property Rights: The Regulation of Innovation* (Oxford University Press, second edition, 2011), p39. As to the adjustment of economic tools, such as the SSNIP test, for market definition in the case of two-sided markets, see generally Florence Thépot, ‘Market Power in Online Search and Social Networking: A Matter of Two-Sided Markets’, (2013) 36(2) *World Competition* 195, pp.215-216.

customers and price discrimination.<sup>126</sup> In *Microsoft/Skype* merger case, the EU Commission left the exact product market definition as an open question since the proposed merger did not cause competition concerns even on the narrowest possible product market.<sup>127</sup> The Commission, according to its preliminary conclusion, considered that, firstly, IM market should not be further segmented by *functionality* because, from the perspective of consumers, a user experience which integrates a range of communication functionalities has been increasingly demanded and in fact the users can easily switch, immediately and without extra cost, between three main communication functions.<sup>128</sup> Secondly, though most IM products are possible to be used on all types of *platforms* (such as PCs, smartphones, tablets), their features and quality on different platforms are different and only a portion of consumers are equipped with all platforms.<sup>129</sup> Thirdly, segmentation of IM market by *operating systems* is not inappropriate because it is not possible to switch between existing IM services on all of the platforms.<sup>130</sup> Therefore, compared to the broader product market definition that includes micro blog and SNS in *Qihoo/Tencent*,<sup>131</sup> a further segmentation of the IM market in the EU case would be foreseeable if the Commission had to define an exact relevant product market.<sup>132</sup> While a potential narrower product market in the EU case is based on the Commission's belief that the proposed merger did not cause competition concern even on the narrowest possible product market, the Guangdong Court in *Qihoo/Tencent* based the extensive product market definition on its SSNIP assumption which was, as demonstrated above, wrongly applied and exaggerated the substitutability of micro blog and SNS.

### 3.3.3 Relevant geographic market

On the subject of relevant geographic market, the CJEU established the main principle in *United Brands*:

“The conditions for the application of Article [102 TFEU] to an undertaking in a dominant position presuppose the clear delimitation of the substantial part of the Common Market in which it may be able to engage in abuses which hinder effective competition and *this is an*

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<sup>126</sup> Commission Notice on the definition of relevant market for the purposes of Community competition law, (1997) OJ C 372/5, Para 36-43.

<sup>127</sup> Ibid, Para 27.

<sup>128</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 25-28.

<sup>129</sup> Ibid, Para 35-36.

<sup>130</sup> Ibid, Para 40-41.

<sup>131</sup> However, the Supreme Court ruled the micro blog and SNS themselves should not be included in relevant product market mainly due to their different product features, thus rejecting the Guangdong Court's ruling in this respect. See the final judgment, *supra* note 74, pp.86-89.

<sup>132</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 20.

*area where the objective conditions of competition applying to the product in question must be the same for all traders.”*<sup>133</sup>

The General Court maintained in *Tetra Pak II* and *British Airways* that it is sufficient that the competitive conditions in the area to be established as the geographic market are “sufficiently homogeneous” and the competitive conditions are not necessarily to be “perfectly homogeneous”.<sup>134</sup> According to established case law, in dealing with the relevant geographic market definition, reference has been made especially to the government measures,<sup>135</sup> transport costs,<sup>136</sup> technical requirements,<sup>137</sup> consumer preferences,<sup>138</sup> geographic scope of the abusive conducts<sup>139</sup>. The EU Commission relies mainly on the consumers’ preferences and the current geographic pattern of purchases.<sup>140</sup> Insofar as the IM market has been particularly concerned, in *Microsoft/Skype* merger case the EU Commission considered that the geographic market for IM service is, if not worldwide, at least EEA-wide.<sup>141</sup> With respect to the market entry barrier, “there are no legal and technical barriers that restrict the use or trade of communications services worldwide”, therefore these services are provided and sourced globally.<sup>142</sup> From the perspective of consumers, these services are “generally perceived as not different in terms of quality, price, and features worldwide”.<sup>143</sup> Moreover, some respondents in the market investigation claimed that there is no any difference in users’ habits in IM services within the EEA and worldwide.<sup>144</sup> Such conclusion however could not be reached in the Chinese case. In

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<sup>133</sup> Judgment in *United Brands*, 27/76, ECLI:EU:C:1978:22, Para 44. (emphasis added)

<sup>134</sup> Judgment of 6 October 1994, *Tetrapak v Commission*, T-83/91, ECR, ECLI:EU:T:1994:246, Para 91; ; Judgment of 17 December 2003, *British Airways v Commission*, T-219/99, ECR, ECLI:EU:T:2003:343, Para 108.

<sup>135</sup> i.e. Judgment in *United Brands*, ECLI:EU:C:1978:22.

<sup>136</sup> i.e. Judgment of 10 March 1992, *Societa Italiano Vetro SpA, Fabbrica Pisana SpA and PPG Vernante Pennitalia SpA v. Commission*, T-68/89, 77/89 and 78/89, ECR, ECLI:EU:T:1992:38.

<sup>137</sup> i.e. Judgment in *Telemarketing v. CLT*, 311/84, ECLI:EU:C:1985:394.

<sup>138</sup> i.e. Judgment in *Coöperatieve Vereniging Suiker Unie*, 40 to 48, 50, 54 to 56, 111, 113 and 114-73, ECLI:EU:C:1975:174.

<sup>139</sup> i.e. Judgment in *Nederlandsche Banden Industrie Michelin*, 322/81, ECLI:EU:C:1983:313; Judgment in *Hoffmann-La Roche*, 85/76, ECLI:EU:C:1979:36.

<sup>140</sup> See Doris Hildebrand, *The Role of Economic Analysis in the EC Competition Rules* (Kluwer Law International, second edition, 2002), p302. See also Commission Notice on the definition of relevant market for the purposes of Community competition law [1997] OJ C 372/5, Para 47 and 48.

<sup>141</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 66.

<sup>142</sup> *Ibid*, Para 64-65. As to the discussion on the extraterritorial application of EU competition law in establishing jurisdictional competence upon anticompetitive conduct originating in the Internet, see generally Andreas Themelis, ‘The Internet, Jurisdiction and EU Competition Law: The Concept of “Over-territoriality” in Addressing Jurisdictional Implications in the Online World’ (2012) 35(2) *World Competition* 325.

<sup>143</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 65.

<sup>144</sup> *Ibid*.

the first place, apparently the extent of the internet integration between domestic network in mainland China and the outside network is lower than the integration degree between EU's member states, or EU's internet as a whole with the worldwide network. For example, there are legal or *technical* barriers preventing consumers in mainland China from accessing to certain overseas consumer communication services such as those provided by Facebook and Twitter. In the second place, compared to the Commission's broader geographic market definition, it might be more likely that mainland China could constitute a separate IM market geographically, since most consumers in mainland China are inclined to use domestic IM products and competitive threats from overseas IM service providers are thus insignificant even some of them provide IM service in Chinese language.<sup>145</sup> Considering these, the competitive conditions in the mainland China and the outside world might not be sufficiently homogeneous. It is thus questionable to conclude a global IM market in this case merely because of the borderless feature of the internet. If this is the case, it could be deduced that geographically a worldwide market would be automatically established in every anti-monopoly case involving the software industry. Such one-size-fit-all rule would not fit for every case. Hence, the final judgment of the Supreme Court held that, rather than a worldwide IM market, the geographic market in this case should be defined to include only the region of mainland China.<sup>146</sup>

### 3.3.4 Dominant position

According to the analysis of dynamically competitive industries in Chapter 2,<sup>147</sup> a general conclusion that software markets are more likely to generate market power than old economy industries may not be reached.<sup>148</sup> Such perspective has been accepted by the Supreme Court. According to the final decision, the Supreme Court held that in the dynamically competitive industries, for instance those internet-related markets, assessment of a dominant position merely by market share might be misleading, and the possession of a dominant position could not be directly inferred by the high market share.<sup>149</sup> Rather, in these fast growing sectors where the market boundary is far from clear compared to traditional industries, the Supreme Court maintained that more attention should be paid to other factors, *inter alia* market entry

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<sup>145</sup> See China Internet Network Information Centre's *China Instant messaging User Research Report* (2009), available at <http://www.cnnic.net.cn/hlwfzyj/hlwxyzbg/201106/P020120709345301865898.pdf>, last visited on 29 October 2013, p14,

<sup>146</sup> The final judgment, *supra* note 74, pp.94-97.

<sup>147</sup> See chapter 2, section 4.2.2.

<sup>148</sup> See Cecilio Madero Villarejo, 'Abuses of a Dominant Position in Information Technology Industries (IT)', in Claus Dieter Ehlermann and Isabela Atanasiu (eds) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?* (Hart Publishing, 2006), p526.

<sup>149</sup> The final judgment, *supra* note 74, pp. 98-99.

barriers.<sup>150</sup> In *Microsoft/Skype* merger case, the EU Commission observed that, generally, the IM market is a newly growing sector where the services provided are shifting from PCs to other devices.<sup>151</sup> Secondly, IM services users are sensitive to the price charged for the services provided since most of the IM services are offered for free, therefore a high degree of innovation is essential for the competitors to expand the consumer base.<sup>152</sup> Thirdly, also because of the ‘free of charge’ feature, market shares in volume (active users in a specified period of time) could act as a better proxy than market shares in value to indicate market power.<sup>153</sup> Fourthly, the barriers to entry and expansion of the IM market are not high, even taking into account the existence of the network effects.<sup>154</sup> While in the assessment of relevant product market the EU Commission concluded that the IM market should not be distinguished by *functionality*,<sup>155</sup> in the phase of competitive assessment the Commission examined the proposed merger by the types of functionality respectively, namely text messaging, voice calls and video calls.<sup>156</sup> After evaluating the market power of notified parties on each type of communications services, the Commission concluded that even in the segment of consumer video calls services where Microsoft would have strongest position with a combined market share of [80-90]% after the proposed transaction,<sup>157</sup> the proposed merger would not significantly impede effective competition in the internal market.<sup>158</sup> This was based on the Commission’s observations on the IM market’s characteristics, which gave rise to the finding that market power enjoyed by Microsoft would not allow him to slow down the pace of innovation or lower the quality of services provided.<sup>159</sup>

It is noteworthy that, as mentioned above, on the one hand the EU Commission *implied* that only the providers who offer the whole range of functionalities could be regarded as effective competitors to the notified parties, on the other hand the Commission assessed the combined market power of notified parties in *each* type of functionality. Thus, when calculating the market shares in the phase of competitive assessment, the segmentation of consumer communications services by functionality also included the market shares of some providers

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<sup>150</sup> Ibid.

<sup>151</sup> COMP/M.6281 – Microsoft/Skype, *supra* note 79, Para 69-74.

<sup>152</sup> Ibid, Para 77, 81-84.

<sup>153</sup> Ibid, Para 78-80.

<sup>154</sup> Ibid, Para 89-95.

<sup>155</sup> Ibid, Para 28.

<sup>156</sup> Ibid, Para 110-131.

<sup>157</sup> Ibid, Para 109.

<sup>158</sup> Ibid, Para 131.

<sup>159</sup> Ibid, Para 120-130.

offering only one or two types of communication services, who should not be viewed as effective competitors in the phase of market definition. Such inconsistency appears to be acceptable, since in assessing market power the Commission aimed to demonstrate that even in the narrowest relevant product segment, the post-transaction market power enjoyed by Microsoft would not raise serious competition concern.

However, this enlargement approach in the phase of competitive assessment in *Microsoft/Skype* case could not be applied in the phase of defining relevant product market in the *Qihoo/Tencent* case where the Guangdong Court identified micro blog and SNS as interchangeable products to comprehensive IM software. On the one hand, like the *Microsoft/Skype* case, the Guangdong Court observed that the relevant product at issue should be the comprehensive IM software that offers main types of communications functionalities such as text messaging, voice calls and video calls. On the other hand, the Court subsequently regarded micro blog and SNS as interchangeable products to comprehensive IM software, and explained that consumers would switch to micro blog and SNS if the comprehensive IM software started to charge. While the available micro blog and SNS in the area of mainland China could not provide whole range of functionalities in terms of IM services, such inconsistent criteria used are not well-grounded. Therefore, they should not have been identified as effective competitive constraints as Facebook and Google+ (although not being comprehensive IM software, these sites could offer whole range of instant communications functionalities) in the EU *Microsoft/Skype* case. That may explain why the Supreme Court ruled the micro blog and SNS themselves should not be included in relevant product market mainly due to their different product features, thus rejecting the Guangdong Court's ruling in this respect.<sup>160</sup>

Although the courts' decisions in *Qihoo/Tencent* are not fully convincing particularly on the IM market boundary issue, the judgments of *Qihoo/Tencent* have shed some light particularly on the definition of relevant product and geographic market in software industry against the scant judicial experience since the enactment of the AML in China. Also, the unique economic features and profit mode of the IM market have been taken into consideration by the courts in assessing the market power. Prior to the adoption of any AML guidance in the IP context, this case has demonstrated Chinese courts' confirmative answer to the *pre-question* – whether in abuse cases involving IPRs the prohibitions of the AML are only applied to activities conducted by undertakings with a dominant position. Definitely the possession of a dominant position is a premise even in such fast growing sectors before assessing allegedly abusive conduct's effect on competition. Though in some parts of the first instance judgment of the Guangdong Court

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<sup>160</sup> The final judgment, *supra* note 74, pp.86-89.

and the final judgment of the Supreme Court (to a lesser degree though) came to the conclusions without convincing reasoning, they still represents the Chinese courts' state-of-the-art understanding as to how the competition rules should be applied in a more economic way, particularly in those dynamically competitive industries.

#### **4. Assessing refusal to license: substantial criteria in draft**

As summarized in the beginning of the case study of *Qihoo/Tencent*, the ambiguity of Article 55 of the AML leaves a number of questions unanswered, *inter alia* whether an unconditional and unilateral refusal to license would constitute an abuse of dominant position (the *first question*), the obligation competition authority would impose on the IPR holder after his refusal to license has violated anti-monopoly rules (the *second question*), and whether refusal to license IPR would be equally treated as refusal to conclude other contracts (the *third question*). After investigating the *pre-question* – the necessity of the possession of a dominant position in IPR-related cases, it is now possible to address these substantial concerns and examine the substantial criteria to assessing the refusal to license behaviour which is in process of ongoing discussion. The answers to these three questions will be provided in this part and the next part. While the *second question* is a follow-on issue, which will be the next part's subject about the remuneration rate setting once IPR holder's refusal to license behaviour has been found abusive, this part will answer the *first* and *the third question*. The purpose of this part is to investigate whether and under what conditions an unconditional and unilateral refusal to license IPR in China would constitute abuse of dominant position. In other words, despite the fact that the AML is modelled after EU competition law in many respects as demonstrated in chapter 1<sup>161</sup>, this part aims to explore whether potential Chinese competition criteria on refusal to license will be akin to EU's 'exceptional circumstances test', or it will take a position like the US where "antitrust liability for mere unilateral, unconditional refusals to license patents will not play a meaningful part in the interface between patent rights and antitrust protections"<sup>162</sup>.

##### **4.1 Microsoft interoperability information case in China**

The on-going SAIC's investigation against Microsoft for alleged breach of the AML is so far the only Chinese competition case where an undertaking may be found to have violated the Chinese competition rules by, among other practices, refusing to disclose interoperability information. In June 2013, after receiving a complaint from an unnamed company which

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<sup>161</sup> See chapter 1, section 2.

<sup>162</sup> US Department of Justice and Federal Trade Commission, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (2007), p32.

alleged that Microsoft had violated China's competition law in relation to problems with compatibility, bundling and document authentication for its Windows operating system and Microsoft Office software, the SAIC started to inspect the practices of Microsoft, and the latter submitted report on these issues to the SAIC.<sup>163</sup> However, the SAIC considered that the preliminary proceeding could not address the competition authority's concerns. On 28 July 2014 the SAIC initiated a formal competition investigation against the alleged abusive practices of Microsoft, and raided – carried out by almost 100 staffs from Beijing, Shanghai, Guangdong, Sichuan, Fujian, Hubei, Jiangsu, Chongqing and Hebei – four of the software company's office in Beijing, Chengdu, Guangzhou and Shanghai. During the raids the SAIC officers interviewed Microsoft's senior managers and some personnel in the marketing and finance departments, seized two computers, copied some internal communicating documents, emails, contracts and financial reports.<sup>164</sup>

On 4 August 2014 the SAIC questioned Microsoft deputy General Counsel Mary Snapp, and issued a sternly worded statement warning Microsoft not to, by any means, impede the authority's investigation.<sup>165</sup> On 6 August 2014 the SAIC conducted another round of raids at Microsoft's one unnamed office that was not involved in the first raid, and Accenture Information Technology (Dalian), to whom Microsoft outsources financial work.<sup>166</sup> On 1 September 2014, the SAIC questioned Microsoft Vice President David Chen, and issued a statement requiring Microsoft within 20 days to make a written explanation to reply to the queries on the compatibility of its Windows operating system and Office software.<sup>167</sup> On 25 September 2014, the Director-General of the SAIC Mao Zhang, in a meeting with Microsoft CEO Satya Nadella, pledged a fair and transparent investigation and stated that questions and suggestions from the company about the investigation are welcome, while on the Microsoft side the chief executive promised to fully cooperate with Chinese authorities in their competition law investigation.<sup>168</sup>

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<sup>163</sup> See SAIC's press release, available at [http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201407/t20140729\\_147122.html](http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201407/t20140729_147122.html), last visited on 22 September 2014.

<sup>164</sup> Ibid.

<sup>165</sup> See SAIC's press release, available at [http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201408/t20140804\\_147293.html](http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201408/t20140804_147293.html), last visited on 22 September 2014.

<sup>166</sup> See SAIC's press release, available at [http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201408/t20140806\\_147358.html](http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201408/t20140806_147358.html), last visited on 22 September 2014.

<sup>167</sup> See SAIC's press release, available at [http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201409/t20140901\\_147993.html](http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201409/t20140901_147993.html), last visited on 22 September 2014.

<sup>168</sup> See SAIC's press release, available at [http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201409/t20140926\\_148715.html](http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201409/t20140926_148715.html), last visited on 30 September 2014.



In light of SAIC's high-profile investigation against Microsoft – including particularly, among others, two rounds of raids at Microsoft's offices carried out by more than 100 staffs, and questioning or meeting with several Microsoft's top executives – and its harsh tone clearly reflected in its published statements, it appears that Microsoft is very likely, if not certainly, to be found as having abused its dominant position by aforementioned behaviour if the American firm cannot convince or settle with the authority. Put the possible outcome of the investigation aside, it might be more interesting to anticipate what substantial criteria would be adopted by the SAIC in assessing Microsoft's allegedly abusive refusal to disclose interoperability information. Against the backdrop of the empty Article 55 of the AML, in order to explore the substantial competition criteria and possible treatment against particular practice of the right owner with a dominant position, one has to consult the draft *Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights* ('the draft AML IP Guideline' or 'the draft Guideline')<sup>169</sup> and the draft *Implementing Rules on the Prohibition of Abuses of Intellectual Property Rights for Purposes of Eliminating or Restricting Competition* ('the draft IP Enforcement Regulation' or 'the draft Regulation')<sup>170</sup>. To implement Article 55 of the AML, timely guidance “akin to the Federal Trade Commission and U.S. Department of Justice's 1995 IP Guidelines or the European Commission's Transfer of Technology Block Exemption Regulation” should be formulated.<sup>171</sup> According to the AML, competition guidelines should be laid down by the Anti-Monopoly Committee.<sup>172</sup> The Anti-Monopoly Committee – without explaining the reason for its choice – assigned the drafting work of the AML IP Guideline to the SAIC Task Force, who formulated the AML IP Guideline draft and has modified the draft for four times until 2012. From the end of 2012 the SAIC suspended the drafting of the AML IP

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<sup>169</sup> The fifth draft AML IP Guideline was released in the International Symposium of Forefront Issues of Anti-Monopoly Law Enforcement on 14 August 2012. An unofficial English translation is available as an appendix to the Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights, available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014.

<sup>170</sup> The latest version of the IP Enforcement Regulation was released by the SAIC on 10 June 2014 for public comments, available at [http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610\\_145803.html](http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610_145803.html), last visited on 20 July 2014. The drafting process is introduced in the following text. All the relevant articles of the draft IP Enforcement Regulation in the following text are translated by the author himself.

<sup>171</sup> Darren S. Tucker, 'Inside the Latest Draft of SAIC's IP Antitrust Rules', *Law 360*, 6 August 2013, available at <http://www.law360.com/competition/articles/461987/inside-the-latest-draft-of-saic-s-ip-antitrust-rules>, last visited on 27 March 2014.

<sup>172</sup> AML, *supra* note 12, Article 9.

Guideline and turned to draft the IP Enforcement Regulation, which will be binding in SAIC's proceedings in non-price related cases. In 2013 the SAIC issued two IP Enforcement Regulation drafts.<sup>173</sup> During the sixth EU-China Competition Week (18-20 March 2013, Beijing), EU experts (including Mr Lucas Peeperkorn, policy analyst from DG Competition, and Dr Edward Smith, director and senior economist of services from the Office of Fair Trading of the UK) and Chinese officials discussed the content of the first draft of the IP Enforcement Regulation in a roundtable discussion. Among others, participants exchanged views on questions such as whether intellectual properties could be regarded as essential facilities in the refusal to license scenario, and what are the criteria for establishing an abusive refusal to license IPR.<sup>174</sup> The second draft was issued on 18 September 2013 and circulated within a limited number of government officials, scholars and practitioners for comments.<sup>175</sup> The SAIC released the latest draft of the IP Enforcement Regulation for public comments on 10 June 2014, attached with a file explaining the drafting process of the Regulation and summarizing some of its significant provisions ('the Explanatory Notes').<sup>176</sup> In the Explanatory Notes the SAIC has admitted that the IPR-competition interface is such a complicated and sensitive area that it is immature to formulate a comprehensive AML IP Guideline, therefore the IP Enforcement Regulation will be firstly laid down.<sup>177</sup> The SAIC has stated in its 2014 anti-monopoly enforcement priorities that the discussion of the draft IP Enforcement Regulation would be finished before the end of 2014, but it appears the SAIC is not thus bound to adopt the regulation in 2014.<sup>178</sup> Hence, it is far from clear when the drafting of the AML IP Guideline, which primarily bases on the experience obtained in implementing the IP Enforcement Regulation, will be re-started.

## 4.2 AML IP Guideline (fifth draft)

### 4.2.1 Relevant articles in general provisions

The draft AML IP Guideline starts with the relationship between intellectual property laws and

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<sup>173</sup> Since the IP Enforcement Regulation is different with the IP guideline in the sense that the draft regulation has binding effect and only applies to non-price related behaviour of undertakings, it is inappropriate, as reportedly sometimes, to name these two drafts as 'the sixth AML IP Guideline' and 'the seventh AML IP Guideline'.

<sup>174</sup> See <http://www.euchinacomp.org/index.php/competition-weeks?id=278>, last visited on 25 April 2014. However, EU competition law experts' comments on this draft IP enforcement regulation in general, and their comments on the refusal to license IPR provision in particular, have not been publicly available.

<sup>175</sup> The second draft of SAIC's IP Enforcement Regulation has not been publicly available.

<sup>176</sup> Both the draft for comment and the explanatory notes are disclosed by the SAIC in the same notice, address see *supra* note 170.

<sup>177</sup> See The Explanatory Notes, *supra* note 170, point 2.

<sup>178</sup> [http://www.saic.gov.cn/ywdt/gsyw/sjgz/xxzx\\_1/201401/t20140122\\_141398.html](http://www.saic.gov.cn/ywdt/gsyw/sjgz/xxzx_1/201401/t20140122_141398.html), last visited on 26 April 2014.

the AML in Article 2. Despite the second paragraph that reduplicates the content of Article 55 of the AML, the first paragraph of Article 2 of the draft Guideline clarifies the objectives commonly shared by IP laws and competition law.<sup>179</sup> Like internationally prevailing practice, it states that though IP laws and competition law have different roles and approaches, they share the same fundamental goals of promoting innovation and efficiency, and enhancing consumer welfare and public interests.<sup>180</sup> These general principles provide important guidance for the decision-makers and the public to understand the interrelation between IP protection and the AML.

Concerning the contribution of intellectual property to a dominant position, Article 9 provides that “antimonopoly law enforcement agencies treat intellectual property rights *in the same manner* as other property rights”, therefore an undertaking possessing IPRs should not be presumed as holding a dominant position in the relevant market.<sup>181</sup> According to the draft Guideline, in cases where IPRs involved constitute an important or even crucial factor for an undertaking to gain market power, relevant provisions within the AML should be relied on by the enforcement authorities to identify, or to presume the existence of a dominant position.<sup>182</sup>

In assessing IPR holder’s conduct in a given situation, this draft Guideline requires the AML enforcement authorities to weigh the anti-competitive impact and the pro-competitive impact brought about by the behaviour of the IPR holder.<sup>183</sup> The anti-competitive or possible anti-competitive impact on competition could be the elimination or restriction of existing competition, or the elimination or restriction of potential competition in the relevant market. The former could be either the decrease of the number of competitors in the relevant market caused by conducts such as the acquisition of IPRs or the arrangement of exclusive licenses, or the reduced degree of competition between existing competitors through conducts such as cross-licensing agreement.<sup>184</sup> The latter impact would prevent other existing competitors from obtaining resources on reasonable terms and potential competitors from entering into the market through IPR holders’ behaviour such as *refusing to license*, controlling key technology and other resources, or imposing or raising market entry barriers.<sup>185</sup> On the other hand, it is the IPR holder that undertakes the burden of proof to demonstrate that the pro-competitive impacts

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<sup>179</sup> The AML IP Guideline (fifth draft), *supra* note 169, Article 2, Para 1.

<sup>180</sup> *Ibid.*

<sup>181</sup> *Ibid.*, Article 9, Para 1. (emphasis added)

<sup>182</sup> *Ibid.*, Article 9, Para 2.

<sup>183</sup> *Ibid.*, Article 11.

<sup>184</sup> *Ibid.*, Article 11, Para 1.

<sup>185</sup> *Ibid.*

originated from such conduct outweigh the anti-competitive impacts.<sup>186</sup> The actual or potential pro-competitive impacts stand for the efficiency improvement in production or resource utilization through innovation and technology dissemination.<sup>187</sup> This Article further provides that, to prove such actual or potential efficiency improvement, the IPR holder should demonstrate following conditions are met:

- “(1) The improvement in efficiency is objective and can be proved;
- (2) The restrictive act of the intellectual property right holder is indispensable to the production of efficiency;
- (3) The efficiency generated must be capable to be shared by consumers;
- (4) The restrictive act of the intellectual property right holder will not substantially restrict competition in the relevant market.”<sup>188</sup>

In assessing the anti- and pro-competitive effects of IPR holder’s behaviour, the draft Guideline suggests enforcement authorities to mainly consider the following factors: (1) the IPR holder, the trading counterparties and the competitors’ market positions; (2) the concentration degree of the relevant market; (3) the market entry and exit barriers; (4) the industry practices and the degree of industrial development; (5) the length and scope of IPR holder’s exercising behaviour; (6) the impact on promoting innovation and disseminating technology; (7) the IPR holder’s innovative capability and his pace of technological upgrade.<sup>189</sup>

#### **4.2.2 Specific articles related to refusal to license**

In the same manner as Article 17 of the AML that provides a non-exhaustive list of prohibited abusive behaviour, Article 16 of the draft Guideline prohibits undertakings with a dominant position, which is achieved largely through their possession of IPRs, from adopting a set of IPR-related abusive conducts. Refusal to license IPR, as long as there is no due justification, like other prohibited behaviour – such as setting unfairly high licensing fee, abusive tying of IPR products, is enumerated as illegal behaviour by an IPR holder with a dominant position.<sup>190</sup> Following this general prohibition provision, Article 17 of this draft Guideline aims specially at refusal to license IPR issue, providing more detailed guidance by stating that:

“The ‘refusal to license intellectual property rights’ referred to in Subsection (2) of Article 16 of this Guide refers to a refusal by intellectual property rights holders to license intellectual

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<sup>186</sup> Ibid, Article 11, Para 3.

<sup>187</sup> Ibid, Article 11, Para 2.

<sup>188</sup> Ibid.

<sup>189</sup> Ibid, Article 10.

<sup>190</sup> Ibid, Article 16, item 2.

property rights to other undertakings for reasonable use. The refusal to license is a form of exercising a rights holder's intellectual property rights. Under normal circumstances, the State Council Antimonopoly Law enforcement agencies will not impose an obligation on intellectual property rights holders to transact with competitors or trading counterparts.

In the course of an undertaking's exercise of its intellectual property rights, the State Council Antimonopoly Law enforcement agencies generally will not deem an undertaking's unilateral refusal to license to other undertakings a violation of the Antimonopoly Law when that refusal is unconditional or non-discriminatory. However, refusals to license intellectual property rights that fall under one of the following categories may be deemed by the State Council Antimonopoly Law enforcement agencies to be a violation of the Antimonopoly Law's provision on the abuse of an undertaking's dominant market position:

- (1) Undertakings with dominant market positions unfairly, discriminatorily refuse to license their intellectual property rights;
- (2) The intellectual property right refused to be licensed by the undertaking with a dominant market position is an essential facility for the licensee to compete in the relevant market, such that the refusal to license that intellectual property right will prohibit the licensee from competing effectively in the relevant market, which will adversely impact competition and innovation in the relevant market, and result in consumer needs not being able to be satisfied.”<sup>191</sup>

This Article starts with a general principle, which is consistent with EU practice, that non-discriminatory or unconditional refusal to license IPR normally would not infringe the AML. Then this Article provides two exceptions to the general principle: discriminatory refusal to license exception, and the ‘essential facility exception’. The latter is the subject of this research. Apart from the requirement of possession of a dominant position, to establish an abusive refusal to license IPR, the ‘essential facility exception’ provision as shown above proposes that three cumulative conditions should be satisfied. Firstly the IPR at issue is an essential facility for the requesting party. Secondly due to the refusal the requesting party will not be able to compete effectively in the relevant market. Thirdly the refusal has adversely impact on the competition and innovation in the market, which could be demonstrated by the unmet consumer demands.

While the AML does not include any reference to the essential facility doctrine, this doctrine has been firstly recognized in SAIC's *implementing rules on prohibition of abuses of dominant*

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<sup>191</sup> Ibid, Article 17.

*market position*.<sup>192</sup> As one form of abusive refusals to deal, Article 4(5) of SAIC's implementing rules prohibits the undertaking with a dominant position from refusing the counterparty's request for using the essential facility under reasonable conditions.<sup>193</sup> It states that in assessing an allegedly abusive refusal to allow requesting party to use an essential facility the enforcement authority will take into account the feasibility of separately investing and developing such facility, degree of the requesting party's reliance on such facility for its business, the possibility of the facility holder making such facility accessible, and the impact on the facility holder's own operation if he makes access to his facility available.<sup>194</sup> However, SAIC's implementing rules has neither clarified the definition of 'the essential facility', nor has it addressed whether such prohibition applies to refusal to license scenario. It appears that the draft Guideline has, for the first time, extended the application of essential facility doctrine to the area of IPRs.

### **4.3 IP Enforcement Regulation (draft for comment)**

#### **4.3.1 General provisions**

The draft IP Enforcement Regulation contains more or less the same provisions in terms of non-price related behaviour.<sup>195</sup> Like Article 9 of the draft Guideline, Article 6 of the draft Regulation also provides that the investigation of whether the IPR holder possesses a dominant market position should be conducted in line with relevant provisions of the AML (namely

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<sup>192</sup> Provisions for the Industry and Commerce Administrations on the Prohibition of Abuse of Dominant Market Position, *supra* note 63.

<sup>193</sup> Ibid, Article 4. ("A business operator with a dominant market position is prohibited to refuse to deal with its counterparty in any of the following forms without justifiable reasons: 1. Reducing the current trading volume with the counterparty; 2. Deferring or terminating a current transaction with the counterparty; 3. Refusing to have new transactions with the counterparty; 4. Imposing restrictive conditions which makes it difficult for the counterparty to continue trading with the business operator; or 5. Refusing the counterparty's request for using its necessary facilities under reasonable conditions in the course of production and operation. For finding a violation under Item (5), factors such as the following shall be considered comprehensively: feasibility in separately investing in and building or developing such facilities, degree of the counterparty's reliance on such facilities for effective production and operation, possibility of the business operator making such facilities available, and its impact over the production and operation of the business operator.")

<sup>194</sup> Ibid.

<sup>195</sup> See D. Daniel Sokol and Wentong Zheng, 'FRAND in China', (3 February 2014), p11, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2335664](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2335664), last visited on 26 March 2014. Compared to the AML IP Guideline, the improvements contained in the SAIC IP Enforcement Regulation (earlier draft) see generally Darren S. Tucker, 'Inside the Latest Draft of SAIC's IP Antitrust Rules', *Law 360*, 6 August 2013, available at <http://www.law360.com/competition/articles/461987/inside-the-latest-draft-of-saic-s-ip-antitrust-rules>, last visited on 27 March 2014.

Article 18 and 19<sup>196</sup>), and that the IPR held by the undertaking may serve as a important factor in assessing the holder's dominant position rather than a decisive factor according to which a dominant position could be presumed.<sup>197</sup>

In assessing impact of IPR holder's behaviour on competition, the draft Regulation has a similar article with minor differences as its counterpart within the draft Guideline, providing that the SAIC will consider the following factors: (1) the IPR holder and its trading counterparties' market positions; (2) the concentration degree of the relevant market; (3) the market entry and exit barriers; (4) the industry practices and the degree of industrial development; (5) the length and scope of constraints brought about by IPR holder's exercising behaviour; (6) the impact on promoting innovation and disseminating technology; (7) the IPR holder's innovative capability and his pace of technological upgrade; and (8) other factors related to examining the impact of IPR holder's behaviour on competition.<sup>198</sup> Compared to the provision in the draft Guideline, it should be noted that the market position of the competitors has been removed from the specified factors which should be taken into consideration. It is unknown whether such removal implies that the market position of the competitors would be treated as irrelevant in assessing the effects of IPR holder's behaviour on competition in non-price related cases (including refusal to license cases), or it makes no difference since this factor would still be taken into consideration as 'other relevant factor' by the SAIC in a given case.

Within the provisions regarding the general analytical framework, one would notice a

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<sup>196</sup> Article 18 of the AML reads as follows: "The dominant market position of a business operator shall be determined according to the following factors: 1. The market share of the business operator and its competitive status in the relevant market; 2. The ability of the business operator to control the sales market or the raw material supply market; 3. The financial and technological conditions of the business operator; 4. The extent of reliance on the business operator by other business operators in the transactions; 5. The degree of difficulty for other business operators to enter the relevant market; and 6. Other factors relevant to the determination of the dominant market position of the business operator."

Article 19 reads as follows: "Under any of the following circumstances, a business operator may be presumed to have a dominant market position: 1. The market share of one business operator accounts for 1/2 or more in the relevant market; 2. The joint market share of two business operators accounts for 2/3 or more in the relevant market; or 3. The joint market share of three business operators accounts for 3/4 or more in the relevant market. Under the circumstance prescribed in Item 2 or 3 of the previous paragraph, if any of the business operators has a market share of less than 1/10, that business operator shall not be considered to have a dominant market position. A business operator that has been presumed to have a dominant market position shall not be considered as having a dominant market position if the operator can provide opposite evidence."

<sup>197</sup> The IP Enforcement Regulation (draft for comment), *supra* note 170, Article 6, Para 2.

<sup>198</sup> *Ibid*, Article 18.

significant change with respect to the efficiency defence. According to the draft Guideline, the burden of proof to demonstrate efficiency is upon the dominant undertakings, who should provide all the evidence necessary to satisfy a series of requirements to demonstrate the claimed efficiency.<sup>199</sup> But in the draft Regulation, such cumulative requirements to demonstrate the efficiency originated from the allegedly abusive conduct have been deleted. Unlike the draft Guideline, there is no further clarification in the draft Regulation on whether the burden of proof to demonstrate the claimed efficiency is still upon the dominant undertaking or it has been shifted to the enforcement authority.

#### **4.3.2 Specific article related to refusal to license**

The SAIC in the Explanatory Notes stressed that the right owners' unilateral behaviour of refusal to license is, in particular, a sensitive issue.<sup>200</sup> In order to strike a sound balance between encouraging innovations and protecting competition, the lawmakers determined to retain the prohibition but narrow the application – compared to the general prohibition on refusal to deal in the AML<sup>201</sup> – only in the essential facility situations.<sup>202</sup> Article 7 of the draft Regulation provides as follows:

“In the absence of due justifications, the dominant undertakings are prohibited from refusing to license their intellectual property rights to other undertakings under reasonable conditions, if such intellectual property rights constitute an essential facility for the production and operating activities in the relevant market.

In examining whether the intellectual property rights in a given case constitute an essential facility, following factors should be taken into consideration: the intellectual property rights at issue are indispensable for other undertakings to compete in the relevant market, and there is no reasonable alternatives in the relevant market; refusal to license such intellectual property rights will result in negative effects on competition or innovation in the relevant market; licensing such intellectual property rights will not cause unreasonable harm to the right holder (etc.).”<sup>203</sup>

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<sup>199</sup> The AML IP Guideline (fifth draft), *supra* note 169, Article 11.

<sup>200</sup> The Explanatory Notes, *supra* note 170, section 3, point 3.

<sup>201</sup> AML, *supra* note 12, Article 17, item 3.

<sup>202</sup> The Explanatory Notes, *supra* note 170, section 3, point 3.

<sup>203</sup> The IP Enforcement Regulation (draft for comment), *supra* note 170, Article 7. The author would like to point out that ‘etc.’ in Chinese (‘等’) could, depending on different contexts, either indicate there are other requirements which are not specified, or have no substantial meaning hence could be neglected. Therefore the author, when translating this article from Chinese to English, chose to put the ‘etc.’ in the brackets.



Compared to Article 17 of the draft Guideline, there are some significant changes that could be observed in the latest draft Regulation. First of all, whether discriminatory refusal to license IPR would constitute abuse of dominant position has not been touched upon in the draft Regulation, since the draft Regulation only deals with non-price related IPR issues. On top of that, the draft Regulation has deleted the starting principle declared in the draft Guideline that IPR holder should have the right to choose his trading partners and thus under normal circumstances refusal to license IPR will not be deemed by AML enforcement authority as abuse of dominant position.<sup>204</sup> Unlike the draft Guideline where unconditional refusal to license IPR raises competition concern only in ‘essential facility exception’ circumstances,<sup>205</sup> Article 7 of the draft Regulation has seemingly implied that the Chinese lawmakers has converted prohibition of refusal to license from an exception into a rule by omitting the general principle.

Moreover, while neither the draft Guideline nor the draft Regulation has explicitly given a definition for ‘essential facility’, these two documents structure the ‘essential facility doctrine’ in a different manner. The draft Guideline sets forth three cumulative conditions to find an abusive refusal to license (in addition to the absence of due justifications requirement), in which IPR at issue constituting an essential facility is merely one requirement, and other two requirements are parallel and cumulative.<sup>206</sup> Nevertheless, the draft Regulation directly puts forward that the dominant undertaking is prohibited from refusing to license his IPR as long as the IPR at issue constitutes an essential facility. In other words, apart from the requirement of the absence of due justifications, the IPR requested constituting an essential facility is the only requirement to establish an infringement of the AML. Unlike other two cumulative and parallel conditions in the draft Guideline, firstly in the draft Regulation it remains vague by the text whether the three factors are cumulative. Secondly, these factors are to be considered by the enforcement authority for the purpose of examining whether the IPR at issue constitutes an essential facility, indicating that these factors are to be considered within rather than parallel to

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<sup>204</sup> In Article 17 of the AML IP Guideline (fifth draft), *supra* note 169, it provides that “[t]he refusal to license is a form of exercising a rights holder’s intellectual property rights. Under normal circumstances, the State Council Antimonopoly Law enforcement agencies will not impose an obligation on intellectual property rights holders to transact with competitors or trading counterparts. In the course of an undertaking’s exercise of its intellectual property rights, the State Council Antimonopoly Law enforcement agencies generally will not deem an undertaking’s unilateral refusal to license to other undertakings a violation of the Antimonopoly Law when that refusal is unconditional or non-discriminatory.” See *supra* section 4.1.2.

<sup>205</sup> Article 17 of the AML IP Guideline (fifth draft), *supra* note 169, second paragraph, item 2. See full article in *supra* section 4.1.2.

<sup>206</sup> The AML IP Guideline (fifth draft), *supra* note 169, Article 17.

the ‘essential facility’ requirement.

However, given that there is no definition for ‘essential facility’, the draft Regulation’s mere ‘essential facility’ requirement provides little meaningful guidance for the undertakings. The factors to be considered in examining the existence of an essential facility therefore serve as the substantial criteria in the Regulation’s approach. Regardless of whether the enforcement authority will find the dominant undertaking’s conduct of refusal to license abusive in exceptional situations, by comparing the substantial conditions provided in the draft Guideline with those in the draft Regulation, one could observe that the Chinese lawmakers has adopted a *lower* standard to establish an abusive refusal to license. The substantial conditions in the draft Guideline and the draft Regulation could be labelled, in an EU-like way, as the indispensability condition, the elimination of competition condition, and the impact on the consumers/IPR holder condition. In the first place, as said before, while the conditions in the draft Guideline are apparently cumulative, the manner adopted in the draft Regulation makes it unclear whether the conditions are cumulative or alternative. And it is also vague whether the factors to be considered in the draft Regulation are close-ended like the draft Guideline, or the list is open-ended and the SAIC thus is entitled to take other relevant factors into consideration.<sup>207</sup> In the second place, concerning the indispensability condition, in addition to the requirement in both documents that the IPR at issue is indispensable for other undertakings (including the requesting party) to effectively compete in the relevant market, the draft Regulation demands that within the market there should be no *reasonable* substitutions to the IPR at issue.<sup>208</sup> There is no further guidance on the standard the AML enforcement authority will employ to determine whether another IPR in the relevant market constitutes a *reasonable* substitution to the IPR held by the dominant undertaking. If the enforcement authority adopts a high standard to define the concept ‘reasonable substitution’, the consequence will be that some less competitive IPRs will be ignored and it will result in a lower standard to find the IPR at issue as an essential facility for other undertakings. In the third place, as to the elimination of competition condition, the approach of the draft Regulation requires the anti-competitive effects caused by such refusal on the competition *or* the innovation in the market,<sup>209</sup> while the approach of the draft Guideline demands that the refusal to license should cause negative effects on both of the competition *and* the innovation in the relevant market.<sup>210</sup> Apparently the standard of the draft Regulation is lower since this requirement is satisfied as long as the enforcement authority identifies negative

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<sup>207</sup> As mentioned in *supra* note 203, the ‘etc.’ in Chinese may be interpreted in two different ways.

<sup>208</sup> The IP Enforcement Regulation (draft for comment), *supra* note 170, Article 7, Para 2.

<sup>209</sup> *Ibid.*

<sup>210</sup> The AML IP Guideline (fifth draft), *supra* note 169, Article 17, Para 2(2).

effects either on market competition or on the innovative activities. In the fourth place, the draft Guideline and the draft Regulation have divergent criteria with respect to the impacts on the consumers/IPR holder condition. Whereas the draft Guideline requires that there should be unmet consumer demands due to the refusal conduct<sup>211</sup> which is consistent with the EU practice, the draft Regulation attaches importance to whether the obligation to license would potentially cause unreasonable harm on the right holder.<sup>212</sup> Compared to the consumer welfare condition, from the perspective of the enforcement authority it might be a relatively simple task to prove the non-existence of potentially unreasonable harm on the IPR holder to establish an abusive refusal to license. What is more, the standard in interpreting the term ‘unreasonable harm’ is at the discretion of the enforcement authority.

Taking these dissimilarities between the draft Guideline and the draft Regulation into consideration, it might be possible that quite divergent conclusions could be reached by the SAIC in the China’s Microsoft interoperability information disclosure case depending on which criteria the enforcement authority would like to apply. While by the criteria set by the draft Regulation Microsoft’s refusal to disclose information is highly likely to be treated as abuse of dominance, the software firm will have more chance to exempt from competition law liability if the authority examines its practice against the criteria of the Guideline even the interoperability information is considered to be *de facto* essential facility in the relevant market. Admittedly, this is based on the assumption that both of the envisaged criteria on refusal to license within the draft Guideline and the draft Regulation become effective which the enforcement authority could apply. Therefore, when the Guideline and the Regulation come into effect will be significant for SAIC’s investigation on Microsoft. Considering the aforementioned fact that it is still unknown when the drafting of the AML IP Guideline will be resumed, for Microsoft investigation there may be two possibilities. Either, the draft Regulation remains unchanged in essence and becomes effective sooner than the SAIC delivers its final decision. If this is the case, Microsoft may become the first offender of the Article 7 of the IP Enforcement Regulation. Or, if the SAIC issues its final decision before the effective date of the IP Enforcement Regulation, it is completely unclear as to how the SAIC will interpret the essential facility doctrine to distinguish abusive refusal behaviour from right owners’ lawful exercise of intellectual property rights.

#### **4.4 EU: being a mentor rather than a preacher**

*Terms of Reference of the EU-China Competition Policy Dialogue* states that “every state has

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<sup>211</sup> Ibid.

<sup>212</sup> The IP Enforcement Regulation (draft for comment), *supra* note 170, Article 7, Para 2.

the right to develop its own model to adjust to its unique economic, legal and political environment.”<sup>213</sup> The publicly available materials of the activities held under the framework of the EU-China Competition Dialogue<sup>214</sup> have demonstrated that, in exporting the EU competition law model, EU has taken a “gradual and systematic” strategy by “respecting rather than criticising” the AML.<sup>215</sup> During the fifth EU-China Competition Week which was held in October 2012, EU Commission official Lucas Peeperkorn explained and advocated how Article 102 TFEU has been applied by the EU Commission and the EU courts in the IPR-related cases, particularly EU’s approach in refusal to license scenario.<sup>216</sup> However, the EU-China Competition Dialogue’s informal nature seemingly would result in EU’s weakness in exporting its competition law norms into China. Therefore, it might be unavoidable that China is in the process of establishing its own competition law rules with norms that are picked and chosen from EU competition law, rather than imitating the whole model of EU competition law in every respect.<sup>217</sup>

The design within the draft Guideline and the draft Regulation in terms of the substantial criteria to assessing dominant undertaking’s conduct of refusal to license is such a case where, rather than entirely copying the EU approach, Chinese lawmakers appear to import from the EU practice by picking and choosing from EU competition law norms. Some scholars criticized the broad *essential facility* provision in the draft Guideline because it goes beyond what is required under the US and the EU competition law.<sup>218</sup> However, through above comparison between the refusal to license provision in the draft Guideline and that of the draft Regulation, it could be observed that, despite the differences with EU’s ‘exceptional circumstances test’

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<sup>213</sup> *Terms of Reference of the EU-China Competition Policy Dialogue*, see [http://ec.europa.eu/competition/international/bilateral/cn2b\\_en.pdf](http://ec.europa.eu/competition/international/bilateral/cn2b_en.pdf), last visited on 20 January 2014.

<sup>214</sup> See <http://www.euchinacomp.org/index.php/zh/%E7%AB%9E%E4%BA%89%E6%94%BF%E7%AD%96%E5%91%A8>, last visited on 10 April 2014.

<sup>215</sup> Qianlan Wu, ‘EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law?’ (2012) 18(3) *European Law Journal* 461, pp.468-470.

<sup>216</sup> [http://www.euchinacomp.org/index.php/zh/?option=com\\_content&view=article&id=256](http://www.euchinacomp.org/index.php/zh/?option=com_content&view=article&id=256), last visited on 10 April 2014.

<sup>217</sup> Qianlan Wu, ‘EU-China Competition Dialogue: A New Step in the Internationalisation of EU Competition Law’ (2012) 18(3) *European Law Journal* 461, p475.

<sup>218</sup> See D. Daniel Sokol and Wentong Zheng, ‘FRAND in China’, (3 February 2014), footnote 31, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2335664](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2335664), last visited on 26 March 2014; Darren S. Tucker, ‘Inside the Latest Draft of SAIC’s IP Antitrust Rules’, *Law 360*, 6 August 2013, available at <http://www.law360.com/competition/articles/461987/inside-the-latest-draft-of-saic-s-ip-antitrust-rules>, last visited on 27 March 2014.

which will be analyzed below, the criteria in the draft Guideline is the one that is closer to the EU approach. Firstly, like what has been confirmed by EU courts in a number of cases,<sup>219</sup> the provision within the draft Guideline provides a similar general principle that it is at the discretion of the right holder to license, or otherwise to refuse to license, its IPR to a third party, including its competitors, making abusive refusal to license only in exceptional cases. Secondly, compared to the provision in draft Regulation, the way the provision in the draft Guideline structures the substantial conditions explicitly demonstrates that the three conditions are cumulative, which is akin to the CJEU's position in *IMS Health* case.<sup>220</sup> Thirdly, like EU's 'exceptional circumstances test', in order to establish an exceptional abusive refusal to license the provision in the draft Guideline also takes into account the indispensability of the IPR requested, the impacts brought about by the refusal on market competition and innovation, and the existence of unmet consumer demand.

Nevertheless, even though the substantial approach in the draft Guideline appears closer to the EU approach compared to the much broader essential facility provision in the draft Regulation, both of them are divergent, to varying degrees, with EU's 'exceptional circumstances test' in many respects. First of all, in the EU the obligation upon the IPR holders to make their rights accessible by other undertakings could only be imposed in cases where, among other exceptional circumstances, there are two neighbouring markets involved.<sup>221</sup> In *IMS Health* the CJEU even ruled that it is sufficient if "a potential market or hypothetical market can be identified".<sup>222</sup> However, there is no 'upstream-downstream markets' requirement either in the draft Guideline or in the draft Regulation, thus remaining the question open as to whether companies in China could force a dominant competitor at the same market level to license essential IPR and compete directly against the licensor.

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<sup>219</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, Para 7-8; Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para. 49; Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para. 34; Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 331.

<sup>220</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 219, Para 38 and Para 52.

<sup>221</sup> See John Temple Lang, 'Anticompetitive Abuses under Article 82 involving Intellectual Property Rights', in Claus Dieter Ehlermann and Isabela Atanasiu (eds) *European Competition Law Annual 2003: What is an Abuse of a Dominant Position?* (Hart Publishing 2006) 589, p610: "in two-market situations because a competitor in the downstream market that gains control of a necessary input is not offering a better or a cheaper product in the downstream market, but only getting power to harm consumers in that market by shutting out its competitors", "in a single market situation, something that is 'necessary' to compete can only be a competitive advantage". See also Andreas Heinemann, 'The contestability of IP-protected markets' in Josef Drexel (ed), *Research handbook on intellectual property and competition law* (Edward Elgar 2008) 54, p59.

<sup>222</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 219, Para 44.

More importantly, unlike the three cumulative conditions in the ‘exceptional circumstances test’ that the CJEU has carefully established to confine abusive refusal to license to exceptional situations, the vague conditions, either in the draft Guideline or in the draft Regulation, provide the enforcement authority too much discretion, making it possible that these conditions might be interpreted in such a broad manner that refusal to license IPR is prohibited as a rule rather than an exception. With regard to the indispensability condition, the provisions in the draft Guideline and the draft Regulation, as demonstrated in the previous section, simply provide that the IPR requested be an essential facility for the requesting party to compete in the relevant market, while EU case law requires that it should not only be undisputed that there is no other available substitutes, even though they may be disadvantageous, but it should also be demonstrated that there are “technical, legal or even economic obstacles capable of making it impossible, or even unreasonably difficult, for any other undertaking alone or in cooperation to potentially establish a substitute”.<sup>223</sup> As to the other two conditions – elimination of competition condition and the new product condition, the General Court has in *Microsoft I*, as elaborated in Chapter 3, adopted lower standards.<sup>224</sup> Regarding the elimination of competition condition, the General Court ruled that it is not necessary to wait until there is no more competition left on the market, and the different terminologies used by the EU Commission – *risk of elimination of competition* and *likely to eliminate competition* – have nothing to do with the standard of assessment for this condition.<sup>225</sup> Thus a likely prediction about the eliminative effect on competition over time would suffice for the competition authorities in the EU.<sup>226</sup> On the new product condition, the CJEU held in *IMS Health* that “the refusal [...] may be regarded as abusive only where the undertaking which requested the licence does not intend to limit itself essentially to duplicating the goods or services already offered on the secondary market by the owner of the intellectual property right, but *intends to produce new goods or services not offered by the owner of the right and for which there is a potential consumer demand*.”<sup>227</sup> Regardless of the precise definition of the ambiguous concept ‘new product’,<sup>228</sup> the General Court in *Microsoft I* added follow-on innovation into the ‘exceptional circumstances test’ and

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<sup>223</sup> Judgment in *Oscar Bronner*, C-7/97, ECLI:EU:C:1998:264, Para 43 and 44.

<sup>224</sup> See chapter 3, section 2.

<sup>225</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, supra note 219, Para 561.

<sup>226</sup> Emil Paulis, ‘Abuses of Dominant Position and Monopolization: Conclusions of the Major Debates in the EU and USA’, in Abel M. Mateus and Teresa Moreira (eds) *Competition Law and Economics: Advances in Competition Policy Enforcement in the EU and North America* (Edward Elgar 2010), p163; Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p901.

<sup>227</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, supra note 219, Para 49. (emphasis added)

<sup>228</sup> See more in chapter 3, section 2.3.1.

replaced the new product condition by a broader notion of *consumer harm*.<sup>229</sup> The General Court maintained that Article 102 TFEU would be infringed not only by practices which prejudice consumers directly, but also by those which indirectly harm their interests.<sup>230</sup> Thus a limitation on technical development of the entire industry deriving from the dominant undertaking's refusal is also within the meaning of Article 102 TFEU. Therefore according to some scholars the judgment of the *Microsoft I* case implies that the right to refuse would thus become an exception rather than a rule.<sup>231</sup> In this regard, Article 17 of the draft Guideline and Article 7 of the draft Regulation have, for one thing, mixed these two EU conditions together; for another, the provisions in the draft Guideline and the draft Regulation appear to be, to varying degrees, close to the lower standards adopted by the General Court in *Microsoft I* case rather than those established by the CJEU in *IMS Health*. For a refusal to license to be treated as abusive, Article 17 of the draft Guideline requires the negative effects brought about by the refusal on the competition, the negative effects also on the innovation, and the existence of unmet consumer demand. Thus, the approach in the draft Guideline, apart from the indispensability condition, is composed of the elimination of competition condition with a much lower standard (requiring merely anti-competitive effects), the *Microsoft I*-like consumer harm condition (requiring broadly the negative effects on innovation and unmet consumer demand). On the other hand, the criteria adopted by Article 7 of the draft Regulation, by requiring merely the negative effects caused by such refusal either on the competition or on the innovative activities, is apparently even lower than that in the draft Guideline.

In addition, the CJEU in *IMS Health* ruled that it is “sufficient” that the three conditions of the ‘exceptional circumstances test’ be satisfied to treat IPR holder’s refusal as abusive,<sup>232</sup> resulting in that the General Court in *Microsoft I* held that “[t]he circumstance relating to the appearance of a new product [...] cannot be the only parameter which determines whether a refusal to license an intellectual property right is capable of causing prejudice to consumers within the meaning of Article [102(b) TFEU]”<sup>233</sup>. In this regard, the seemingly open-ended approach in the draft Regulation is thus akin to the EU situation in the sense that other factors might also be taken into account by the enforcement authority, while the clearly close-ended

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<sup>229</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, *supra* note 219, Para 643-665.

<sup>230</sup> *Ibid*, Para 664.

<sup>231</sup> On this point see also Ian S. Forrester, ‘Magill Revisited’, in Inge Govaere, Reinhard Quick and Marco Bronckers (eds), *Trade and Competition law in the EU and Beyond* (Edward Elgar 2011) 376, p388: “In less than 20 years, we have moved from anything being surprising (*Magill*) to everything being possible (*Microsoft*).” See also Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing 2010), p123.

<sup>232</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, *supra* note 219, Para 38.

<sup>233</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, *supra* note 219, Para 647.

approach adopted by the draft Guideline has demonstrated that the three cumulative conditions are ‘necessary’ to establish an abusive refusal to license IPR.

#### 4.5 Proposal

Before advancing to the modification that could possibly be made in the current analytical framework, one should notice the different roles that should be played by a competition law guideline and an enforcement regulation. The Anti-Monopoly Committee, according to Chinese Legislation Law<sup>234</sup>, is not an eligible body that is empowered to issue law interpretations.<sup>235</sup> Thus, the AML IP Guideline, as a soft law potentially adopted by the Anti-Monopoly Committee, for one thing, has no binding effect on the activities of the AML enforcement authorities even though the guideline has influence on the activities of the enforcement authorities as well as the undertakings. For another, the purpose of the IP Guideline is to *provide detailed guidance* on the analytical frameworks and standards which are already (concisely) provided in existing legislations, but not to *create* its own approaches. Thus, it is right in this regard that the Chinese lawmakers, before adopting the draft IP Guideline, turned to draft the IP Regulation.

Based on such relationship between the IP Guideline and the IP Regulation, it is thus possible to conclude that the IP Regulation should set the tone for the IP Guideline. As to the analytical framework within the IP Regulation related to refusal to license, this thesis recommends revising Article 7 to contain two parts: a general principle and the exceptional circumstances to establish abusive refusals. Firstly, to safeguard the legitimate interests of IPR holders, a general principle like the starting point of the EU competition law (and that in the current draft IP Guideline) should be stated that, in normal circumstances any IPR holders, whether dominant or not, should have the right to choose its trading partners and the AML enforcement authorities will not impose upon the IPR holders an obligation to license their IPRs. Then, it is vital to revise current essential facility provision in the draft Regulation, more or less, into the EU-like exceptional circumstances. It should be noted that there have been two standards in the EU case law. Compared to the stringent criteria established by the CJEU in *Magill* and *IMS Health*, the exceptional circumstances test interpreted by the General Court in *Microsoft I* could chill the

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<sup>234</sup> *The Law on Legislation of the People's Republic of China* (issued and came into effect in 2000, translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=386&lib=law&SearchKeyword=&SearchCKeyword=%c1%a2%b7%a8%b7%a8>, last visited on 15 May 2014.)

<sup>235</sup> *Ibid.*, Article 42.



innovators and thus be criticized.<sup>236</sup> Considering that the current criteria set up in the draft Regulation is even broader than the General Court's *Microsoft I* standard, the desired target EU template should be the *Magill/IMS Health* standard. However, it might be unlikely that the IP Regulation would completely copy the strict criteria set out in *IMS Health*, especially the new product condition due to its ambiguous definition and Chinese lawmakers' attitude reflected in previous drafts. Thus, it may be realistic to re-set the Chinese version of competition criteria on refusal to license in between the EU *Magill/IMS Health* standard and the *Microsoft I* standard. To be specific, this thesis suggests the second part be structured as follows:

Absent due justifications, a refusal to license intellectual property rights would be treated by the enforcement authority as abusive only in exceptional circumstances where the following three conditions are cumulatively met:

- (1) The IPR at issue is indispensable for carrying on a particular business on the downstream market;
- (2) The refusal will eliminate all effective competition on the downstream market;
- (3) The refusal is likely to lead to consumer harm.

Such revision would bring current Article 7 of the draft Regulation closer to the EU practice and enhance legal certainty for one thing. For another, such proposed framework also leaves room for the enforcement authority to use its discretion to employ appropriate standard in a given case. As to the potential IP Guideline, based on the criteria set out in the IP Regulation, more detailed guidance on assessing refusal to license conduct could be provided. The IP Guideline, after obtaining experience from enforcement authority's activities, could summarize the standards that have been adopted by the authority. For example, with respect to the condition of elimination of competition, the IP Guideline could investigate whether the enforcement authority interprets this requirement in a given case with a higher standard like the 'likely to eliminate competition' condition in *IMS Health*, or with a lower standard like the 'risk of elimination of competition' condition in *Microsoft I*. Likewise, concerning the consumer harm requirement, the IP Guideline could also provide guidance for the undertakings as to whether the enforcement authority considers abusive refusal to license only in *IMS Health*-like cases where such refusal has prevented the emergence of a new product for which there is potential consumer demand, or this requirement will be satisfied in a similar manner as the General Court's ruling in *Microsoft I* as long as the technological development in the relevant market has been impaired because of such refusal.

Apart from the substantial criteria to be set out in the final IP Regulation as well as more

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<sup>236</sup> See chapter 3, section 2.5.

detailed guidance provided in the potential AML IP Guideline, the follow-on licensing fee setting could also affect the interests of intellectual property right owners. Chapter 4 has investigated the question of how the dominant undertaking's IPR would be accessed by requesting parties once his unilateral behaviour of refusal to license has been considered as an abuse of dominant position. It has been observed that excessive pricing would raise competition concern in both of the EU and China.<sup>237</sup> It is argued that in the regulated industries – such as energy industries and telecommunication industry – where industry regulators already oversee these industries prior to the enactment of the AML, addressing pricing-related abuses under competition law might not be feasible since this would require competition law enforcement authorities exercise power over industry regulators which may cause inter-agency conflicts.<sup>238</sup> But how about the excessive pricing issue in other industries? The section below investigates the FRAND-related provisions within Chinese competition law system and significant royalty rate setting cases in practice.

## **5. Follow-on issue: FRAND in China**

### **5.1 Excessive pricing and FRAND in the legal instruments**

Within the abuse of dominant position chapter of the AML, Article 17 explicitly prohibits dominant undertakings from selling products at unfairly high prices.<sup>239</sup> The AML however does not make it clear whether this prohibition on excessive pricing could be extended to dominant undertaking's IPR licensing behaviour. Since the draft IP Regulation only covers non-price related IPR issues, so far the draft IP Guideline is the only legal instrument where conduct of setting an excessive licensing fee by dominant undertakings is explicitly prohibited. Article 16 of the draft AML IP Guideline stipulates that intellectual property right owners with a dominant market position are prohibited from licensing their rights at “unfairly high prices”.<sup>240</sup> Unlike other specifically prohibited behaviour such as refusal to license or tying involving IPRs on which there are separate and more detailed provisions, the draft IP Guideline does not provide further criteria for the undertakings as to at which level the dominant undertaking's conduct of setting the licensing fee would amount to charging an unfairly high price. The boundary between an unfairly high price and an acceptable licensing fee is highly

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<sup>237</sup> See the introduction part of chapter 4.

<sup>238</sup> See Wentong Zheng, ‘Transplanting Antitrust in China: Economic Transition, Market Structure, and State Control’, (2010) 32 *University of Pennsylvania Journal of International Law* 643, pp.707-708.

<sup>239</sup> AML, *supra* note 12, Article 17(1).

<sup>240</sup> The AML IP Guideline (fifth draft), *supra* note 169, Article 16(1).

uncertain.<sup>241</sup>

To avoid setting an unfairly high licensing fee, one concern has been raised as to on what principle the IPR holders – the standard-essential-patents (‘SEP’) holders and non-SEP holders – should base to determine the appropriate royalty rate. Like the situation in the EU, the concept of FRAND – *fair, reasonable and non-discriminatory* – is currently one issue in the process of standardization. The FRAND issue has been tackled by both the IP regulator and competition law regulator. The State Intellectual Property Office<sup>242</sup> and the National Standardization Administration Committee<sup>243</sup> issued the *Interim Provisions on the Administration of National Standards Involving Patents*,<sup>244</sup> providing that if the patent holder is willing to include his patent in a national standard, he may license his patent either on a royalty-free basis, or on a FRAND basis.<sup>245</sup> It has not been specified, however, as to what constitutes a FRAND licensing.

From the perspective of competition law regulator, the setting of royalty level appears in both of the draft IP Guideline and the draft IP Regulation. The draft IP Guideline states that, absent due justifications, the SEP holder’s conduct of refusal to license his patented technology to any potential licensee *on reasonable terms* within the process of standardization is an example of abusive behaviour, which is prohibited since it could cause or likely to have anticompetitive effect on the market competition and innovation.<sup>246</sup> The draft IP Guideline then in the same Article requires that once the SEP holder’s patented technology is included into national or industrial standard, the upper limit of the licensing fee set by the SEP holder should not be significantly higher than that charged before such patented technology is included in the

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<sup>241</sup> See Sebastian Evrard and Yizhe Zhang, ‘Refusal to Deal in China: A Missed Opportunity?’ in Adrian Emch and David Stallibrass (eds.) *Review of China’s Anti-Monopoly Law – The First Five Years* (Wolters Kluwer 2013) 135, p139.

<sup>242</sup> The State Intellectual Property Office of the People’s Republic of China (‘SIPO’), directly affiliated to the State Council, is mainly responsible for patent-related administrative work and comprehensively coordination of foreign-related affairs in the field of intellectual property. See more at [http://english.sipo.gov.cn/about/basicfacts/200904/t20090415\\_451001.html](http://english.sipo.gov.cn/about/basicfacts/200904/t20090415_451001.html), last visited on 15 May 2014.

<sup>243</sup> The National Standardization Administration Committee was established by the State Council to undertake administrative management, supervision and coordination of standardization works in China, and represent China in international and regional standardization organizations. See more at [http://www.sac.gov.cn/sac\\_en/introductionofSAC/201011/t20101123\\_4166.htm](http://www.sac.gov.cn/sac_en/introductionofSAC/201011/t20101123_4166.htm), last visited on 15 May 2014.

<sup>244</sup> *Interim Provisions on the Administration of National Standards Involving Patents*, issued by National Standardization Administration Committee and State Intellectual Property Office of China, 19 December 2013, available at [http://www.sipo.gov.cn/zcfg/flfg/zl/bmgfxwj/201401/t20140103\\_894910.html](http://www.sipo.gov.cn/zcfg/flfg/zl/bmgfxwj/201401/t20140103_894910.html) (in Chinese), last visited on 31 March 2014.

<sup>245</sup> Ibid, Article 9 and 10.

<sup>246</sup> AML IP Guideline (fifth draft), *supra* note 169, Article 22, Para 2(4).

standard.<sup>247</sup> Thus in determining a FRAND royalty rate, guidance provided in this Article is applicable only in limited situations where there are directly comparable licensing transactions.<sup>248</sup> On the other hand, the draft IP Regulation is the very legislation where FRAND principle has been officially recognized for the first time in Chinese competition legal system. According to Article 13 of the draft IP Regulation, the dominant undertakings are prohibited from violating their FRAND commitments by refusing other undertakings to implement their SEPs on reasonable terms if there is no due justification.<sup>249</sup>

Thus to some extent the concept FRAND has been established in the SEP-related licensing scenario. However, absent a determined refusal to license case, it is uncertain whether the enforcement authorities will impose upon IP holders an obligation to license on FRAND conditions in non SEP-related scenario (e.g. *de facto* standard) after a refusal to license has been treated as abusive.

## 5.2 Excessive pricing and FRAND in practice

### 5.2.1 Before AML enforcement authorities

Except the SAIC who is in charge of monitoring non-price related behaviour, the NDRC and the MOFCOM are very active in their AML enforcement against the setting of excessive licensing fees. The NDRC is currently investigating InterDigital Corporation ('IDC') and Qualcomm for their allegedly abusive conducts of setting unfairly high licensing fees for Chinese undertakings who need their patents.<sup>250</sup> According to NDRC's official, the investigation of IDC's licensing behaviour, starting by the NDRC from May 2013, has been suspended since the IDC provided a series of commitments to the NDRC, in which, among others, the IDC promises to stop charging Chinese undertakings unfairly high licensing fees and to set its future licensing fees in accordance with the FRAND principle.<sup>251</sup> Another NDRC

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<sup>247</sup> Ibid, Article 22, Para 3.

<sup>248</sup> See D. Daniel Sokol and Wentong Zheng, 'FRAND in China', (3 February 2014), pp.24-25, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2335664](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2335664), last visited on 26 March 2014.

<sup>249</sup> Article 13 of the IP Enforcement Regulation (draft for comment), *supra* note 170, provides, among others, that "[u]ndertakings with dominant market positions, without justifications, shall not engage in the following conducts during the process of standard setting and standard implementation: ... (2) After their patent technology become standard essential patents, *violating the fair, reasonable and non-discriminatory principle and refusing other undertakings to implement such patents on reasonable terms*, or engaging in patent licensing with unfair conditions, or engaging in tying activities during its patent licensing process." (emphasis added)

<sup>250</sup> See NDRC press release, 19 February 2014, available at [http://www.china.com.cn/zhibo/2014-02/19/content\\_31502397.htm](http://www.china.com.cn/zhibo/2014-02/19/content_31502397.htm), last visited on 10 May 2014.

<sup>251</sup> Ibid.

competition law investigation against the licensing practice of the American giant IP holder Qualcomm was started from Nov 2013.<sup>252</sup> According to the latest information disclosed by the Director-General of the NDRC Kunlin Xu at a briefing jointly held by three enforcement authorities on 11 September 2014, NDRC's investigation on Qualcomm's licensing practices, *inter alia* the firm's behaviour of charging allegedly unfairly high licensing fee, is already completed and an infringement decision will be soon delivered.<sup>253</sup>

On top of the enforcement activities of the NDRC targeting past or on-going abusive behaviour, the MOFCOM has also been involved in efforts to prevent prospective excessive licensing fee setting. The *Google/Motorola Mobility* merger case is the first case where the MOFCOM in 2012 mentioned the FRAND principle in its conditional clearance decision, in which, among other conditions, the MOFCOM required that Google should after the transaction continue to undertake Motorola Mobility's FRAND commitments made on the patents originally owned by Motorola Mobility.<sup>254</sup> The *Microsoft/Nokia* merger case<sup>255</sup> demonstrates that the MOFCOM nowadays has paid more attention on prospective excessive licensing fee setting and conduct of refusal to license IPR in the ICT industry. In September 2013 Microsoft and Nokia signed an agreement, according to which agreement Microsoft will acquire Nokia's Devices and Services business subject to regulatory approvals from major jurisdictions such as the US, the EU and China. The MOFCOM mainly investigated the smartphone market, smartphone operating system market and smartphone-related patent licensing market. According to MOFCOM's finding<sup>256</sup>, Microsoft's patents related to Android operating system (SEPs and non-SEPs), are

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<sup>252</sup> Ibid.

<sup>253</sup> See Chinese competition law authorities' briefing on 11 September 2014, available at [http://www.china.com.cn/zhibo/2014-09/11/content\\_33487367.htm?show=t](http://www.china.com.cn/zhibo/2014-09/11/content_33487367.htm?show=t) (in Chinese), last visited on 12 September 2014. It is interesting to note that, according to the Director-General of the NDRC, Qualcomm CEO submitted a report to the NDRC during the second meeting between the authority and the company, and mentioned that one of the authors is Professor Xinzhu Zhang, director of the Research Center for Regulation and Competition at the Chinese Academy of Social Sciences, and also one expert within the Anti-monopoly advisory committee. Afterwards the Anti-Monopoly Committee of the State Council fired him alleging that Zhang accepted money from Qualcomm in exchange for providing testimony favourable to the company in the on-going competition investigation, and such behaviour violated the Committee's internal working rules.

<sup>254</sup> Notice of the MOFCOM's conditional clearance of Google's acquisition of Motorola Mobility (No.25, 2012), 19 May 2012, the decision in Chinese available at <http://fldj.mofcom.gov.cn/article/ztxx/201205/20120508134324.shtml>, last visited on 10 May 2014.

<sup>255</sup> Notice of the MOFCOM's conditional clearance of Microsoft's acquisition of Nokia's Devices and Services business (No. 24, 2014), 8 April 2014, the decision in Chinese available at <http://fldj.mofcom.gov.cn/article/ztxx/201404/20140400542415.shtml>, last visited on 8 April 2014.

<sup>256</sup> The MOFCOM's assessment of the case and the conditions imposed on Microsoft and Nokia, as shown in the following text, are from MOFCOM's decision, see the last footnote.

indispensable for Android smartphone manufacturing industry as they are essential to realizing Android system and important functions of smartphone using Android system. Most of Chinese Android smartphone manufacturers, subject to their technical limitations, could not invent around Microsoft's patents or replace those patents with commercially viable technical solutions. Thus Microsoft is in such a position to intervene the competition in the downstream smartphone market through its Android system-related patents licensing practice. Considering the significance of Microsoft's patents to Android smartphone manufacturing industry, any conduct of refusal to license by Microsoft would substantially prevent competitors from entering into the market, and impair existing competition in the smartphone market in China. Apart from prospective refusal to license conduct, if Microsoft after the transaction raises royalty rates to an unfairly high level, it would have a strong impact on smartphone manufacturers' investment in R&D and sustainable development. Confronted with raised royalty rates, Chinese manufacturers – their average profit margin is relatively low according to MOFCOM's investigation – might either exit the market, or transmit part or whole of the raised costs onto smartphone consumers. Whereas the former would reduce competition in the market, the latter option would directly harm consumer welfare. Concerning the patents related to telecommunication technology, patent holders' refusal to license and raising royalty rates conducts might also have market closure effect or increase manufacturers' costs. A competition concern thus was raised by the MOFCOM that if Nokia after the transaction unreasonably changes the licensing practices with respect to its telecommunication technology SEPs, the overall costs of the smartphone manufacturers would be increased and ultimately consumer welfare would be impaired. On 8 April 2014 MOFCOM finally approved the *Microsoft/Nokia* deal subject to certain conditions. With respect to the SEPs, the MOFCOM mainly required that, among others, the parties to the transaction should abide by the following principles: firstly, the parties should adhere to the FRAND commitments they had made to standard setting organizations; secondly, the parties should not seek an injunction to prevent potential licensees who are willing to implement those SEPs under FRAND conditions; thirdly, the parties should not transfer those SEPs to any other undertaking unless that undertaking agrees to adhere to the principles outlined above.<sup>257</sup> In addition, with respect to Microsoft's licensing practice related to non-SEPs, the MOFCOM demands Microsoft to continue to offer such licenses at royalty rates no greater than those before this transaction or specified in current licensing agreements.

### 5.2.2 Before the courts

The excessive licensing fee issue not only has raised competition concern for the AML

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<sup>257</sup> The English version of the whole commitments provided by Microsoft is available at <http://www.microsoft.com/en-us/news/download/docs/0414chinaannouncement.pdf>, last visited on 10 May 2014.

enforcement authorities, it has also been tackled in private enforcement before the Chinese courts. This could be demonstrated by the recent civil litigation lodged by Huawei against the royalty rate setting practice of InterDigital Corporation ('IDC'), whose licensing practice was also subject to the scrutiny of AML enforcement authority as mentioned in the previous section. The SEP royalty rate dispute between Huawei and IDC, which was the subject of the first instance decision of Shenzhen Intermediate Court<sup>258</sup> and the final decision of Guangdong High Court in appeal<sup>259</sup>, could demonstrate the answer of the Chinese courts to the question of what constitutes a reasonable licensing fee. This is the first and so far the only antimonopoly litigation related to SEP and FRAND royalty setting in China.<sup>260</sup> Huawei sued to Shenzhen Intermediate Court in December 2011, alleging that IDC as an owner of several SEPs for 2G, 3G and 4G telecommunications technologies, had abused its dominant market position by failing to negotiate to license these patents on FRAND terms. These FRAND commitments were required by the intellectual property rights policy of the standard setting organization European Telecommunications Standardisation Institute ('ETSI') when IDC was accepted as a member of ETSI in September 2009. In February 2013, Shenzhen Intermediate Court issued its decision. The first instance judgment found that each SEP in 3G wireless telecommunications industry constitutes an independent patent licensing market, resulting that the SEP holder (IDC in this case) possesses a dominant position in each relevant licensing market.<sup>261</sup> With respect to

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<sup>258</sup> The first instance decision of Shenzhen Intermediate Court has not been published due to business secrets reason. The case facts and the analysis of the court, as will be elaborated below, are generally based on two articles published by the three judges who presided over the case in the first instance trial, Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利权人滥用市场支配构成垄断的认定: 评华为公司诉美国IDC公司垄断纠纷案' ('Determining Whether Standard Essential Patent Holder Abused its Dominant Position: Huawei v. IDC'), *Electronics Intellectual Property Right* (March 2013) 46; Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利使用费纠纷中FRAND规则的司法适用: 评华为公司诉美国IDC公司标准必要专利使用费纠纷案' ('Judicial Application of FRAND Rules in Disputes Involving Royalties for Standard Essential Patent: Huawei v. IDC'), *Electronics Intellectual Property Right* (April 2013) 54. The case summary could see news report, for instance at [http://sztqb.sznews.com/html/2014-01/14/content\\_2753404.htm](http://sztqb.sznews.com/html/2014-01/14/content_2753404.htm), last visited on 1 April 2014.

<sup>259</sup> The final judgment of Guangdong High Court has been publicly available at <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20140417030902158689>, last visited on 20 July 2014. However, the royalty rate-related information in the judgment is not accessible due to business secrets reason.

<sup>260</sup> See Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利权人滥用市场支配构成垄断的认定: 评华为公司诉美国IDC公司垄断纠纷案' ('Determining Whether Standard Essential Patent Holder Abused its Dominant Position: Huawei v. IDC'), *Electronics Intellectual Property Right* (March 2013) 46, p46.

<sup>261</sup> Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利权人滥用市场支配构成垄断的认定: 评华为公司诉美国IDC公司垄断纠纷案' ('Determining Whether Standard Essential Patent Holder Abused its Dominant Position: Huawei v. IDC'), *Electronics Intellectual*

the royalty setting complaint, the court ruled that IDC had violated its FRAND commitment and IDC's conduct had constituted abuse of dominant position by demanding excessive licensing fee.<sup>262</sup> This first instance judgment was affirmed by the Guangdong High Court in October 2013.

The judges stated in their published article with the starting point that, the SEPs holder would violate his FRAND commitment if he directly refuses to license his SEPs to the potential patented technologies implementer who is willing to pay reasonable licensing fee.<sup>263</sup> Concerning the calculation of a FRAND royalty rate, there are two ways to determine a FRAND rate: the approach in theory and the approach in practice. Theoretically, the value of SEPs should be quantified in proportion to their contribution to the profit of the final product, and royalty rates should be allocated among each SEP in line with their varied contribution in an industry standard.<sup>264</sup> However, the judges admitted that such royalty allocation approach is unpractical due to the amount of SEPs involved in a telecommunications industry standard and the lack of a proper method to examine the contribution of each SEP.<sup>265</sup> The judges held that to be a FRAND royalty rate, in practice the licensing fee should be reasonable in itself (the first question), and the licensing fee should be reasonable compared to existing licensing fees negotiated in the same industry as well (the second question).<sup>266</sup> Two general principles should be considered in answering the first question – whether the licensing fee is reasonable in itself. Patent licensing fee should only account for a certain proportion of the profit originated from the final product, since other elements, such as capital, other technologies (including those from other SEPs holders) and licensee's business operation, all have contributed to the profit.<sup>267</sup> The other principle that should be kept in mind is that, the reward the licensor could obtain should be in line with the value of the patent itself, but not resulted from the fact that the patented technology is included in an industry standard.<sup>268</sup> With regard to the second question, it would be rather difficult to answer if there is no comparable licensing fee existed in the same industry.

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*Property Right* (March 2013) 46, pp.48-50.

<sup>262</sup> Ibid, pp.50-52.

<sup>263</sup> See Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利使用费纠纷中FRAND规则的司法适用：评华为公司诉美国IDC公司标准必要专利使用费纠纷案' ('Judicial Application of FRAND Rules in Disputes Involving Royalties for Standard Essential Patent: Huawei v. IDC'), *Electronics Intellectual Property Right* (April 2013) 54, p60.

<sup>264</sup> Ibid, p61.

<sup>265</sup> Ibid.

<sup>266</sup> Ibid.

<sup>267</sup> Ibid.

<sup>268</sup> Ibid.



The judges proposed that the royalty rates should be set roughly at the same level towards equivalent SEPs implementers.<sup>269</sup>

As to the Huawei v. IDC case, the judges held that the following factors should be taken into consideration in the analysis whether the licensing fee proposed by the SEP holder has met the FRAND requirement: the normal profit range in the wireless telecommunication industry, the SEP holder's investment in R&D (including the amount of research personnel) and the quality and quantity of SEPs he possessed, the existing royalty rates negotiated between the licensor and other licensees in the same industry (Apple and Samsung, for instance, in this case), and whether the patented technologies are standard-essential in China or standard-essential worldwide.<sup>270</sup> According to the judges, the licensing fees proposed by IDC to Huawei were much higher than those asked from Apple or Samsung, thus constituting excessive and discriminatory pricing which is prohibited by the AML.<sup>271</sup> It is quite natural, however, to doubt the judges' determination that the assessment of a reasonable royalty rate should take into account the number of SEP holder's research personnel and the quantity of his SEPs, which are apparently not relevant indicators in measuring the value of the SEPs.<sup>272</sup> Shenzhen Intermediate Court, basing on its findings, ordered IDC to cease the alleged excessive pricing. According to publicly available document released by IDC, Shenzhen Intermediate court further ruled that "the royalties to be paid by Huawei for InterDigital's 2G, 3G and 4G essential Chinese patents under Chinese law should not exceed 0.019% of the actual sales price of each Huawei product, without explanation as to how it arrived at this calculation".<sup>273</sup> Therefore, according to publicly available information, it remains unknown as to how the Court figured out this specific rate.

The table 5 below summarizes relevant provisions in (draft) legal documents under Chinese competition law, and relevant opinions in recent public enforcement activities as well as

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<sup>269</sup> Ibid.

<sup>270</sup> Ibid.

<sup>271</sup> See Ruosi Ye, Jianjun Zhu and Wenquan Chen, '标准必要专利权人滥用市场支配构成垄断的认定：评华为公司诉美国IDC公司垄断纠纷案' ('Determining Whether Standard Essential Patent Holder Abused its Dominant Position: Huawei v. IDC'), *Electronics Intellectual Property Right* (March 2013) 46, p51.

<sup>272</sup> See also D. Daniel Sokol and Wentong Zheng, 'FRAND in China', (3 February 2014), p32, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2335664](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2335664), last visited on 26 March 2014.

<sup>273</sup> See InterDigital 2014 Annual Report, 24 February 2014, available at <http://files.shareholder.com/downloads/IDCC/3061303688x0xS1405495-14-10/1405495/filing.pdf>, p26, last visited on 2 April 2014.

significant court judgments with respect to FRAND concept and reasonable royalty rate setting.

		SEPs	Non-SEPs
In legal documents	Draft IP Guideline	1. License on reasonable terms; 2. No significantly higher than that charged before the technology is included in the standard	Unknown
	Draft IP Regulation	Adhere to FRAND commitments	Unknown
In practice	NDRC	Adhere to FRAND commitments, stop charging unfairly high licensing fees	Unknown
	MOFCOM	Adhere to FRAND commitments	No greater than those charged before the transaction or specified in current agreements
	Courts	1. Adhere to FRAND commitments; 2. Calculation of FRAND royalty rate (1) in theory: in proportion to SEPs' contribution to the profit of the final product (2) in practice: two principles a. reasonable in itself: account for a certain proportion of the profit of the final product; in line with the value itself but not the SEP position b. reasonable compared to other existing rates in the same industry	Unknown

Table 5

Source: summarized by the author

Taking into account the analysis of relevant EU practice in Chapter 4<sup>274</sup>, one may come to the following conclusions even from the scattered rules or decisions. First of all, the only royalty rate setting case before the court has demonstrated Chinese judges' EU-like starting point that the royalty rate should be set in line with the economic value of the IPR at issue. Secondly, as pointed out in Chapter 4 that cost-based analysis is not applicable in the context of IP licensing,<sup>275</sup> it is right to exclude this approach in China as well. Thirdly, the judges of *Huawei v. IDC* case held that a reasonable royalty rate should be reasonable in itself and also reasonable compared to available rates in the same industry, echoing the second part of the two-fold approach in *United Brands*.<sup>276</sup> Fourthly, it might also be right to conclude that the General Court's ruling in *Microsoft II*<sup>277</sup> – the remuneration rates should reflect the *intrinsic value* of a technology rather than its *strategic value* – has shed its light upon China, since it has been mentioned, respectively in the draft Guideline, MOFCOM's decision and judges' opinion on *Huawei v. IDC* case, that the royalty rate should not make the IPR holder benefit from the fact that his IPR has been recognized as SEP or from a significant transaction in a non-SEPs situation.

## 6. Institutional issues

On top of transplanting substantial approaches from international successful practice, it is also necessary to seek feasible institutional reforms – which might be no less important in order to ensure consistency and transparency in the enforcement of the Chinese competition law<sup>278</sup> – within current dual AML enforcement system (EU-like administrative agency-oriented public enforcement plus rising private enforcement before the courts) to suit China's unique needs<sup>279</sup> with respect to competition-IP interface in general and the refusal to license issue in particular.

### 6.1 AML enforcement authorities

The selective adaptation of prevailing international practices to suit China's legal and economic context may be tenable in the sense that “foreign practices must be ‘recontextualized’ to

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<sup>274</sup> See chapter 4, section 3.1.1.

<sup>275</sup> Ibid.

<sup>276</sup> Judgment in *United Brands* ECLI:EU:C:1978:22, Para 252.

<sup>277</sup> Judgment of 27 June 2012, *Microsoft v Commission*, T-167/08, ECR, ECLI:EU:T:2012:323.

<sup>278</sup> See H. Stephen Harris and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal’ (2008) 75 *Antitrust Law Journal* 213, pp.227-228.

<sup>279</sup> See generally Mark Furse, ‘Competition Law Choice in China’ (2007) 30(2) *World Competition* 323; Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87.

account for unique institutions and histories.”<sup>280</sup> Taking US antitrust enforcement as an example, the fact that the enforcement of US antitrust rules relies heavily on the regular US courts, causing that it is the changes in the courts’ general procedures rather than the needs of the antitrust system that have resulted in many significant changes in the operation of the system and ultimately have shaped the unique US antitrust enforcement system.<sup>281</sup> The procedural discovery rights for parties have been expanded since the 1940s in the US courts, making the US standard sharply different with those in most other jurisdictions in terms of procedural discovery rights, and having the consequences of “bring[ing] extensive amounts of information to the decisional process”, “affect[ing] the way judges evaluate factual allegations” and “tend[ing] to create far more complex and expensive competition-law litigation than exists elsewhere”.<sup>282</sup> Unlike the situation in the US, China’s administrative agency-oriented system, as elaborated in Chapter 1<sup>283</sup>, is highly unlikely to be replaced by the US court-oriented enforcement style in the near future, since the administrative bureaucracy in China has extensive influence over the overall economic development and also the individual undertakings’ behaviour.<sup>284</sup>

Based on the perception that Chinese decision-makers would pursue the goal of maximizing national interest as a response to a changing economic environment, existing literatures predicted that the AML enforcement activities would aim to protect domestic companies against the competition from multinational companies.<sup>285</sup> However, a recent study has demonstrated that, rather than the protection of national interest, it is *the Chinese bureaucratic structure and policy-making processes* that largely affect the outcome of antitrust enforcement in China.<sup>286</sup> It has been observed that Chinese administrative bureaucracy has adopted the rule

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<sup>280</sup> Nathan Bush, ‘Constraints on Convergence in Chinese Antitrust’ (2009) 54(1) *The Antitrust Bulletin* 87, p97.

<sup>281</sup> David J. Gerber, ‘Constructing Competition Law in China: the Potential Value of European and U.S. Experience’, (2004) 3 *Washington University Global Studies Law Review* 315, p319.

<sup>282</sup> Ibid.

<sup>283</sup> See Chapter 1, section 3.1.

<sup>284</sup> See David J. Gerber, ‘Constructing Competition Law in China: the Potential Value of European and U.S. Experience’, (2004) 3 *Washington University Global Studies Law Review* 315, p330.

<sup>285</sup> See e.g. Nathan Bush and Yue Bo, ‘Disentangling Industrial Policy and Competition Policy in China’, Antitrust Source, Feb. 2011, at 4; Wentong Zheng, ‘Transplanting Antitrust in China: Economic Transition, Market Structure, and State Control’, (2010) 32 *University of Pennsylvania Journal of International Law* 643, pp.671-720; Bruce M. Owen, Su Sun and Wentong Zheng, ‘China’s Competition Policy Reforms: The Anti-Monopoly Law and Beyond’, (2008) 75 *Antitrust Law Journal* 231, pp.242-247, 252-254; H. Stephen Harris, Jr. and Rodney J. Ganske, ‘The Monopolization and IP Abuse Provisions of China’s Anti-Monopoly Law: Concerns and A Proposal’, (2008) 75 *Antitrust Law Journal* 213, pp.224-226.

<sup>286</sup> See Angela Huyue Zhang, ‘Bureaucratic Politics and China’s Anti-Monopoly Law’, forthcoming in *Cornell*

of “management by exception” to make economic policy, meaning that the decision will be referred to a higher administrative authority unless decision-makers make decisions by a rule of consensus.<sup>287</sup> This method directly results in the consequence of fragmented power in policymaking and implementation.<sup>288</sup> With regard to the AML enforcement, according to Angela Huyue Zhang’s research, the personnel composition of the Anti-Monopoly Committee suggests that in this consulting and coordinating organization no single ministry has decisive power and thus the decision-making process is “in effect a consensus-building process” like economic policymaking in China.<sup>289</sup> Taking MOFCOM’s enforcement activities as an example, according to that research, MOFCOM’s consulting practice in merger review, for instance consulting the NDRC or the Ministry of Industry and Information Technology for their opinions and comments,<sup>290</sup> is widely accepted practice within the Chinese administrative bureaucracy known as ‘huiqian’ (meaning countersign in English) to obtain opinions and comments from other government agencies to mitigate the risk that a decision will negatively affect other agencies’ interests.<sup>291</sup> Thus this ‘huiqian’ procedure, which is not unusual among ministerial agencies, is regarded as “an important consensus-building mechanism”.<sup>292</sup>

Moreover, Angela Huyue Zhang’s research has demonstrated that the *incentive structure* of government officials at the central level is the answer to the question why the NDRC appears more aggressive in AML enforcement.<sup>293</sup> Since the incentive structures of the officials of the AML enforcement authorities at the central level are affected by the their departments’ policy control which is tied to the career prospects of those officials, competition law enforcement is merely an instrument for them to fulfil their ultimate career goal – to gain more power within

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<sup>287</sup> See Susan L. Shirk, *The Political Logic of Economic Reforms in China* (University of California Press 1993), pp.116-117.

<sup>288</sup> See Angela Huyue Zhang, ‘Bureaucratic Politics and China’s Anti-Monopoly Law’, forthcoming in *Cornell International Law Journal*, vol. 48, issue 1, latest version available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2391187](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2391187), last visited on 23 May 2014, p18.

<sup>289</sup> *Ibid*, p19.

<sup>290</sup> See D. Daniel Sokol, ‘Merger Control under China’s Anti-Monopoly Law’, *Minnesota Legal Studies Research Paper* No. 13-05 (January 2013), p10, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2207690](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2207690), last visited on 17 March 2014.

<sup>291</sup> See Angela Huyue Zhang, ‘Bureaucratic Politics and China’s Anti-Monopoly Law’, forthcoming in *Cornell International Law Journal*, vol. 48, issue 1, latest version available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2391187](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2391187), last visited on 23 May 2014, pp.19-20.

<sup>292</sup> *Ibid*, p20.

<sup>293</sup> *Ibid*, p24.

the scope of their responsibilities.<sup>294</sup> The NDRC, as the central agency that primarily relies on direct government intervention to perform its designated task of macro-economic management and price control, has been observed to employ the AML enforcement as a powerful tool to pursue its own interest and gain back its power which has been weakened due to the market liberalization.<sup>295</sup> Therefore, if current enforcement system remains, it is suggested that more internal checks and balances be introduced into the enforcement regime for institutional reform purpose.<sup>296</sup>

According to current AML enforcement power division<sup>297</sup>, the competence over unconditional refusal to license IPR behaviour is conferred on the SAIC. Even though the SAIC has played the essential role in formulating the draft AML IP Guideline on behalf of the Anti-Monopoly Committee and the draft IP Regulation for its own implementation of the AML in cases where IPRs are involved, it is questionable whether the SAIC officials own sufficient knowledge and experience to handle complex IPR-involved competition cases where extensive econometric and statistical analysis is needed in many cases. One should keep in mind that by far the SAIC at the central level has merely engaged in three abuse of dominant market position investigations since the enactment of the AML, of which two investigations are still on-going.<sup>298</sup> In addition, since the SAIC only scrutinizes non price-related refusal to license, under current enforcement system it could not continue to monitor IPR holders' follow-on royalty setting practice. Moreover, confronted with other inter-authority and intra-authority

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<sup>294</sup> Ibid, pp.25-26.

<sup>295</sup> Ibid, pp.29-31.

<sup>296</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, pp.654-655.

<sup>297</sup> AML enforcement power division and power struggle through the legislative process see chapter 1, section 3.1.

<sup>298</sup> According to information disclosed by top officials of Chinese competition law enforcement authorities in the briefing held on 11 September 2014, there have been 3 cases registered in the SAIC at the central level, of which one investigation against certain domestic undertaking (name undisclosed) was already suspended and two against foreign undertakings – Tetra Pak and Microsoft – are still in progress. The written record of this official briefing is available at [http://www.china.com.cn/zhibo/2014-09/11/content\\_33487367.htm?show=t](http://www.china.com.cn/zhibo/2014-09/11/content_33487367.htm?show=t), last visited on 12 September 2014. The SAIC announced its investigation against the allegedly abusive behaviour of Tetra Pak on 5 July 2013. According to a short statement made by the SAIC, more than 20 provincial and municipal AICs are involved in the investigation, which has been launched in response to complaints received by the SAIC in recent years about the company's alleged abuse of its dominant position in relation to liquid food packaging, including through bundling practices and preferential treatment. See press release 'SAIC: Tetra Pak is suspected of abusing its dominant market' ('工商总局: 利乐涉嫌滥用市场支配地位被立案调查'), 5 July 2013, available at [http://www.gov.cn/jrzq/2013-07/05/content\\_2441372.htm](http://www.gov.cn/jrzq/2013-07/05/content_2441372.htm), last visited on 10 May 2014. The Microsoft investigation see *supra* section 4.1.

problems as analyzed in Chapter 1<sup>299</sup>, it is urgent to carry out reform of AML enforcement authorities through organization restructuring.

To guarantee enough organizational independence and enormous amount of resources, many Chinese, non-Chinese scholars and practitioners propose to establish an EU-like, independent AML enforcement authority under the State Council at the ministry level.<sup>300</sup> However, it would be very hard to design a new institution under the current organizational structure in order to improve the efficiency of enforcement.<sup>301</sup> It is predicted that “the lack of independence and qualification of its workers will undermine its strength and capability” even if the new AML enforcement authority is granted by future legislation special administrative position directly under the Premier who is the head of the State Council.<sup>302</sup>

Therefore, this thesis suggests a two-phase institutional reform. Firstly, from the long-term perspective it is necessary to establish a single independent competition law enforcement authority, which is also admitted by top officials of Chinese competition law authorities.<sup>303</sup> Nevertheless, based on Angela Huyue Zhang’s finding that the AML enforcement authorities’ decision-making process is a consensus-building process, merging the three competition law divisions under the MOFCOM, the NDRC and the SAIC into one single, EU Commission-like enforcement authority would involve multi-party’s interests and thus be not feasible in the foreseeable future. As a result, the establishment of a single EU Commission-like enforcement authority should be realized in the second phase as the ultimate goal of AML institutional reform. Then, given that the ideal option – merging three authorities into one – is not practical in the near future, this thesis proposes that the institutional reform in the first phase should

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<sup>299</sup> See chapter 1, section 3.2.

<sup>300</sup> Bruce M. Owen, Su Sun and Wentong Zheng, ‘China’s Competition Policy Reforms: The Anti-Monopoly Law and Beyond’ (2008) 75 *Antitrust Law Journal* 231, pp.261-262. See also Maher M Dabbah, ‘The Development of Sound Competition Law and Policy in China: An (Im)possible Dream’, (2007) 30(2) *World Competition* 341, pp.356-357; Jared A. Berry, ‘Anti-Monopoly in China: A Socialist Market Economy Wrestles with Its Antitrust Regime’ (2005) 2 *International Law and Management Review* 129, p150; Yong Huang, ‘Pursing the Second Best: The History, Momentum, and Remaining Issues of China’s Anti-Monopoly Law’ (2008) 75 *Antitrust Law Journal* 117, p125; Jacob S. Schneider, ‘Administrative Monopoly and China’s New Anti-Monopoly Law: Lessons from Europe’s State Aid Doctrine’ (2010) 87 *Washington University Law Review* 869, p894.

<sup>301</sup> Youngjin Jung and Qian Hao, ‘The New Economic Constitution in China: A Third Way for Competition Regime’ (2003) 24(1) *Northwestern Journal of International Law & Business* 107, pp.159-160.

<sup>302</sup> *Ibid*, p160.

<sup>303</sup> See Chinese competition law authorities’ briefing on 11 September 2014, available at [http://www.china.com.cn/zhibo/2014-09/11/content\\_33487367.htm?show=t](http://www.china.com.cn/zhibo/2014-09/11/content_33487367.htm?show=t) (in Chinese), last visited on 12 September 2014.



pursue the second best – merging the two competition law divisions under the NDRC and the SAIC into one agency in charge of non-merger cases.

Such short-term institutional reform is tenable for the following reasons. Firstly, such institutional design might be reasonable in terms of the types of competition law cases. While the difference between merger cases and non-merger cases is more visible, assigning price-related cases and non price-related cases to two agencies is more or less artificial. Since an undertaking might be involved in a mixture of allegedly anti-competitive conducts which include price-related behaviour and also non price-related behaviour,<sup>304</sup> and it is not always that easy to identify whether the behaviour at issue is price-related or non price-related,<sup>305</sup> therefore a potential conflict of jurisdiction might take place between the NDRC and the SAIC under current enforcement power division. The proposed first-phase institutional design could overcome such inter-agency problem.

Secondly, such institutional design might be reasonable in terms of the roles played by the enforcement authorities. As one difference between the MOFCOM and other two authorities, it has been observed that the MOFCOM is more liberal and pro-market.<sup>306</sup> While the MOFCOM provides *ex ante* control, both of the NDRC and the SAIC examine agreements that are already concluded or dominant undertakings' conducts that are already taken. Furthermore, such institutional reform will not change the present way the MOFCOM and other two authorities allocate their administrative resources. While the MOFCOM keeps all decision-making power at the central level, the way the NDRC and the SAIC decentralize their AML enforcement power to corresponding agencies at the provincial level could be remained by the new agency. Thus the set-up of the new agency would not fundamentally alter the resource distribution for all three authorities.

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<sup>304</sup> See Angela Huyue Zhang, 'The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective' (2011) 56(3) *The Antitrust Bulletin* 631, p641; Xiaoye Wang, 'The New Chinese Anti-Monopoly Law: A Survey of a Work in Progress' (2009) 54 *The Antitrust Bulletin* 579, p590.

<sup>305</sup> See Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p264; Xiaoye Wang, 'Three Year's Enforcement of Anti-Monopoly Law in China and the Rule by Law', in Professional Committee on Competition Policy and Law (PCCPL) China Society for World Trade Organization Studies (CWTO) (ed) *Report on Competition Law and Policy of China 2011* (Law Press, China, 2012) 30, p33; Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p104; Mark William, Chapter 4 'China' in Mark William (ed) *The Political Economy of Competition Law in Asia* (Edward Elgar 2013) 88, p113.

<sup>306</sup> See Angela Huyue Zhang, 'Bureaucratic Politics and China's Anti-Monopoly Law', forthcoming in *Cornell International Law Journal*, vol. 48, issue 1, latest version available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2391187](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2391187), last visited on 23 May 2014, pp.26-31.

Thirdly, such design might be reasonable in terms of the establishment of a well-structured competition law legislation system. This first phase reform is sound in the sense that the institutional change does not require any modification of the AML provisions, which will take much time. For instance, the difference in the judicial review procedure between merger cases and non-merger cases in the AML provisions<sup>307</sup> could still apply after the first phase institutional reform. Moreover, merging the competition law divisions of the NDRC and the SAIC would facilitate drafting of AML implementing rules and guidelines for non-merger competition issues. This advantage would be obvious in drafting the AML IP Guideline as well as the IP Regulation. The drafting work of IP Guideline would be expected to be accelerated, since the lawmakers could temporally remove the merger-related provisions from the IP Guideline, and focus on other IPR issues in non-merger situations which are after the institutional reform monitored by the new authority. As to the IP Regulation, it is not necessary any more for the lawmakers to expel price-related articles from the draft IP Regulation. With regard to the existing AML implementing rules, after the reform the new agency could review and integrate the rules originally adopted by the NDRC and the SAIC, which could solve the inconsistency problem within existing implementing rules<sup>308</sup>.

Fourthly, examination of the refusal to license conduct could benefit particularly from the merge of competition law divisions under the NDRC and the SAIC, since in that case not only the refusal behaviour itself but also the follow-on royalty rate setting issue could be scrutinized by the same agency.

Lastly, if it is unlikely to set one new independent agency by incorporating the two competition law divisions under the NDRC and the SAIC, in the first phase of institutional reform merging the competition law function of one authority into the other should be otherwise pursued. To this purpose, merging SAIC's competition law team into the NDRC's might not be recommended option. Considering the NDRC's main task of macro-economy management in general, and the fact that the Industry Coordination Bureau – the bureau formulating industrial policy and coordinating industry planning, the Price Supervision and Anti-monopoly Bureau, and the Price Bureau are allocated to the same deputy director within the NDRC structure,<sup>309</sup> it

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<sup>307</sup> Article 53 of the AML, see analysis in chapter 1, at page 44-45.

<sup>308</sup> For the inconsistent provisions with existing NDRC and SAIC's implementing rules, see examples given in analyzing the first inter-authority problem, in chapter 1, section 3.2.1.

<sup>309</sup> NDRC, Main responsibilities of Zucui Hu, available at <http://huzucui.ndrc.gov.cn/zggz/>, last visited on 18 March 2014.

is questionable whether industrial policy considerations to some extent will be taken into account in a given IPR-related case. Due to the lack of procedural transparency<sup>310</sup>, if the NDRC takes the lead it may “dress up” its decisions – which are in fact driven by industrial policy considerations – as if they are based on competition related considerations.<sup>311</sup> Therefore, merging NDRC’s competition law team into the SAIC’s appears to be a better option.

## 6.2 Before the courts

Since 1994, the Chinese Supreme Court has permitted to establish IPR tribunals within competent Chinese courts.<sup>312</sup> In fact, before the release of that circular, the Beijing Intermediate and High Courts, as the first two courts in the country, established IPR tribunals in August 1993. In October 1996, the Supreme Court set up its IPR tribunal.<sup>313</sup> By the end of 2012, 420 IPR tribunals have been established in China.<sup>314</sup> The Supreme Court in April 2008 enacted its *Provisions on the Cause of Action of Civil Cases*<sup>315</sup>, granting the jurisdiction over anti-monopoly cases to the IP tribunals of competent Chinese courts. Later in July 2008, the Supreme Court distributed the *Circular on Carefully Studying and Implementing the Anti-Monopoly Law*<sup>316</sup> within the Chinese court system, reiterating IP tribunals’ jurisdiction over IP-related anti-monopoly cases and other anti-monopoly cases. Judges in the IP tribunals

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<sup>310</sup> It should be pointed out that on 2 September 2014, the NDRC for the first time published the full decisions in Zhejiang Car Insurance Catel case imposing combined fines of RMB 110 million (USD 17.89 million) on a local trade association in Zhejiang province and 23 property insurance companies for their price fixing behaviour, decisions (in Chinese) are available at <http://jjs.ndrc.gov.cn/fjgld/index.html>, last visited on 10 October 2014.

<sup>311</sup> D. Daniel Sokol and Wentong Zheng, ‘FRAND in China’, (3 February 2014), pp.8-9, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2335664](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2335664), last visited on 26 March 2014.

<sup>312</sup> See *Circular of the Supreme People’s Court on Further Strengthening the Judicial Protection of Intellectual Property Rights* (No. 111 [1994] of the Supreme People’s Court, issued on 29 September 1994), available by subscription at <http://vip.chinalawinfo.com/newlaw2002/slc/slc.asp?db=chl&gid=10608> (in Chinese, last visited on 3 December 2013).

<sup>313</sup> See the Supreme Court’s *Intellectual Property Protection by Chinese Courts in 2009 (White Paper 2009)*, English version available at [http://www.court.gov.cn/zscq/bhcg/201004/t20100426\\_4545.html](http://www.court.gov.cn/zscq/bhcg/201004/t20100426_4545.html), last visited on 3 December 2013.

<sup>314</sup> See the Supreme Court’s *Intellectual Property Protection by Chinese Courts in 2012 (White Paper 2012)*, English version available at [http://www.court.gov.cn/zscq/bhcg/201304/t20130426\\_183662.html](http://www.court.gov.cn/zscq/bhcg/201304/t20130426_183662.html), last visited on 3 December 2013.

<sup>315</sup> *Provisions on the Cause of Action of Civil Cases* (Adopted and issued by the Chinese Supreme Court on 4 February 2008, amended on 18 February 2011). (Translation available by subscription at <http://www.lawinfochina.com/display.aspx?id=8607&lib=law&SearchKeyword=&SearchCKeyword=%C3%F1%CA%C2%B0%B8%BC%FE%B0%B8%D3%C9%B9%E6%B6%A8>, last visited on 20 January 2014)

<sup>316</sup> *The Circular on Carefully Studying and Implementing the Anti-Monopoly Law* (issued by the Supreme Court on 28 July 2008, available at <http://vip.chinalawinfo.com/newlaw2002/slc/slc.asp?db=chl&gid=107282> (in Chinese), last visited on 20 January 2014.)

are perceived to be equipped with more experience and particularly sensitive to the unique features of IPR when approaching IPR-related anti-monopoly cases.<sup>317</sup>

**As to the judicial review**, based on the publicly available information, since the enactment of the AML no defendant has lodged judicial review of any administrative decision made by the Chinese competition authorities.<sup>318</sup> Moreover, it remains unknown whether the judges in the IP tribunals – who are in charge of civil antitrust litigations – will also be designated to hear the administrative cases, or the judges in the administrative tribunals will handle the judicial review of administrative decisions. The expertise of the latter, who generally hear administrative cases in Chinese court system, has been doubted whether they are equipped with sufficient legal and economic knowledge related to competition law allowing them to conduct substantial economic analysis in competition cases.<sup>319</sup> **As to the private enforcement of the AML**, more than 100 civil cases have been handled since the AML came into effect.<sup>320</sup> It has been believed that the AML apparently rely on the administrative enforcement system rather than the judicial system to handle anti-monopoly cases.<sup>321</sup> Nevertheless, Chinese judges have become more confident in conducting economic reasoning and analysis in competition law cases.<sup>322</sup> Recently in some significant competition cases Chinese judges, by delivering relatively long judgments (much longer than publicly available administrative decisions issued by the AML enforcement authorities), have demonstrated their ability of applying competition rules in civil litigations.<sup>323</sup>

The Shanghai No.2 Intermediate Court in 2008 established the first specialized competition law panel, which hears not only civil competition litigations but also the judicial review cases.<sup>324</sup>

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<sup>317</sup> See Nathan Bush, 'Constraints on Convergence in Chinese Antitrust' (2009) 54(1) *The Antitrust Bulletin* 87, p109.

<sup>318</sup> See Angela Huyue Zhang, 'Bureaucratic Politics and China's Anti-Monopoly Law', forthcoming in *Cornell International Law Journal*, vol. 48, issue 1, latest version available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2391187](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2391187), last visited on 23 May 2014, p9.

<sup>319</sup> *Ibid*, p12.

<sup>320</sup> See Xiaoye Wang and Adrian Emch, 'Five Years of Implementation of China's Anti-Monopoly Law – Achievements and Challenges', (2013) 1(2) *Journal of Antitrust Enforcement* 247, p263.

<sup>321</sup> See Bruce M. Owen, Su Sun and Wentong Zheng, 'China's Competition Policy Reforms: The Anti-Monopoly Law and Beyond' (2008) 75 *Antitrust Law Journal* 231, p264.

<sup>322</sup> See David S. Evans, Vanessa Yanhua Zhang and Howard H. Chang, 'Analyzing Competition Among Internet Players: Qihoo 360 v. Tencent', *CPI Antitrust Chronicle*, May 2013 (1).

<sup>323</sup> E.g. Qihoo v. Tencent (IM market case, Guangdong High Court), Huawei v. IDC (FRAND royalty case, Shenzhen Intermediate Court), Rainbow v. Johnson & Johnson (RPM case, Shanghai High Court).

<sup>324</sup> See press release at [http://news.xinhuanet.com/legal/2008-12/23/content\\_10546455.htm](http://news.xinhuanet.com/legal/2008-12/23/content_10546455.htm), last visited on 10 May 2014.

Following Shanghai's initiative, The Chengdu Intermediate Court in 2009 set up the second specialized competition law panel, which is the first in the west China.<sup>325</sup> For countries in the transition like China which is in its early competition enforcement period, normally it is not recommended to count on existing courts to enforce competition law.<sup>326</sup> Some scholars have proposed China should establish specialized competition law courts equipped with more independent judges who are "sufficiently trained in competition law and related economic concepts to develop Chinese competition law in a normative, consistent manner".<sup>327</sup> The need for such specialized courts is particularly significant in IPR-related cases, since those cases such as refusal to license behaviour, unlike other more straightforward competition law cases, require sophisticated understanding of both competition rationales and IP knowledge.

However, it seems the proposal of setting specialized competition law courts might not be adopted in the near future due to the officially proposed specialized IP courts. Under current court system, the task for IP tribunals to handle IP-related litigations (including competition law cases) has become much more difficult due to the sharply increasing case amount<sup>328</sup> and the more complicated and novel questions engaged in those cases.<sup>329</sup> During the second revise process of Chinese patent law in 2000, the State Intellectual Property Office and other relevant departments studied the possibility of establishing specialized IP appellate court, without much progress however at that time. Establishing IP courts has been put on the schedule again since the third revision of the patent law in 2005.<sup>330</sup> According to the decision of the third plenary session of the 18<sup>th</sup> Central Committee of the Communist Party of China which was held in

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<sup>325</sup> See press release [http://news.xinhuanet.com/newscenter/2009-04/22/content\\_11232360.htm](http://news.xinhuanet.com/newscenter/2009-04/22/content_11232360.htm), last visited on 10 May 2014.

<sup>326</sup> See H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, pp.227-228.

<sup>327</sup> H. Stephen Harris and Rodney J. Ganske, 'The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and A Proposal' (2008) 75 *Antitrust Law Journal* 213, pp.227-228. See also Giacomo Di Federico, 'The New Anti-monopoly Law in China from a European Perspective', (2009) 32(2) *World Competition* 249, p268.

<sup>328</sup> According to IP Protection White Paper 2013, *supra* note 4, in 2013 Chinese courts at all levels received more than 89,000 first instance IP civil cases and completed more than 88,600 first instance IP civil cases; as to second instance and retrial IP civil cases, Chinese courts at all levels together received more than 12,000 cases and completed more than 11,800 cases. Among others, courts received 72 first instance antimonopoly civil cases and completed 69 cases in 2013.

<sup>329</sup> See Song Li, 'China planning to establish IPR courts, but the Supreme Court has no timetable now' (最高法：知识产权法院建设正推进，尚无时间表)，available at <http://news.sina.com.cn/c/2014-04-26/151230016961.shtml>, last visited on 26 April 2014.

<sup>330</sup> *Ibid.*

2013,<sup>331</sup> China will “strengthen the application and protection of intellectual property rights (IPR), improve the technological innovation incentive mechanism”, and the possibility of setting up specialized IP courts is being taken into consideration.<sup>332</sup> Compared to IP tribunals, specialized IP courts would be beneficial to solving the problem of shortage of judicial resources for IP cases, enhancing efficiency and legal certainty, and saving judicial costs.<sup>333</sup> On 31 August 2014, the Standing Committee of the National People’s Congress issued the *Decision on Establishment of the Intellectual Property Courts in Beijing, Shanghai and Guangzhou*. (‘the IP Courts Decision’)<sup>334</sup> According to the IP Courts Decision, IP courts will have jurisdiction over first instance civil and administrative IP cases that are technically complex, such as patent, new varieties of plants, integrated circuit layout design and know-how related issues.<sup>335</sup> With regard to IP courts’ jurisdiction over these first instance cases, the IP Courts Decision provides that the IP courts have trans-regional jurisdiction, which may be exercised within the provinces (or municipalities) where the IP courts are located within the first three-year trial period since the establishment of the IP courts.<sup>336</sup> Moreover, the IP courts will have jurisdiction over appeals for the first instance civil and administrative IP judgments relating to copyright and trademark issues made by the basic courts located in the municipalities to which the IP courts belong.<sup>337</sup>

With establishing of IP courts on the agenda of the court system reform, the IP courts will be the fourth type of specialised courts with its own personnel within China’s court system, along with the Maritime courts, Military courts and Railway Transport courts. At present detailed timetable for the establishment of these three IP courts has not been disclosed. More importantly, one question that arises, under the subject of this research, is whether IP tribunals’

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<sup>331</sup> *Decision of the Communist Party of China (CPC) Central Committee on Some Major Issues Concerning Comprehensively Deepening the Reform*, adopted in the third Plenary Session of the 18<sup>th</sup> CPC Central Committee in Beijing, 12 November 2013, available at [http://www.china.org.cn/chinese/2014-01/17/content\\_31226494.htm](http://www.china.org.cn/chinese/2014-01/17/content_31226494.htm), last visited on 1 April 2014.

<sup>332</sup> *Ibid*, point 13 “deepening reform of the management system for science and technology”, Para 2.

<sup>333</sup> Opinion expressed by Nankai University Professor Shanhong Qi in his interview with a Chinese journal *Outlook Weekly*, see Song Li, ‘China planning to establish IPR courts, but the Supreme Court has no timetable now’ (最高法：知识产权法院建设正推进，尚无时间表), available at <http://news.sina.com.cn/c/2014-04-26/151230016961.shtml>, last visited on 26 April 2014.

<sup>334</sup> *Decision on Establishment of Intellectual Property Courts in Beijing, Shanghai and Guangzhou*, adopted by the Standing Committee of the National People’s Congress on 31 August 2014, full decision (in Chinese) available at [http://www.npc.gov.cn/npc/xinwen/2014-09/01/content\\_1877042.htm](http://www.npc.gov.cn/npc/xinwen/2014-09/01/content_1877042.htm), last visited on 12 September 2014.

<sup>335</sup> *Ibid*, Article 2.

<sup>336</sup> *Ibid*.

<sup>337</sup> *Ibid*, Article 3.

competence over competition cases will also be overtaken by the IP courts. The IP Courts Decision leaves it unclear whether competition law cases in general, or those competition law cases relating to IP issues in particular, are qualified as technologically complex and technically specialized cases over which the IP courts should have jurisdiction in the same manner as those explicitly listed in the Decision such as patent disputes. Provided that the answer is affirmative, it remains also unknown whether, after the first three-year trial period, the three IP courts' trans-regional jurisdiction over competition would be extended to cover other regions of China, or other provinces (or municipalities) will be allowed to set up their own IP courts.

## 7. Conclusion

This chapter examines whether the EU approach on refusal to license could be transplanted, or is being considered by Chinese lawmakers. The state-of-the-art understanding of Chinese courts on the relevant market definition and dominant position assessment, particularly in dynamically competitive industries, has been investigated through the study of *Qihoo/Tencent* case. After examining in detail the IPR-related provisions within the existing competition law, and the envisaged substantial criteria on refusal to license within the draft AML IP Guideline and the draft IP Enforcement Regulation, the analysis demonstrates that the proposed analytical framework within the draft AML IP Guideline and the draft IP Enforcement Regulation towards refusal to license is such a case where, rather than entirely copying the EU approach, Chinese lawmakers appear to import from the EU practice by picking and choosing from EU competition law norms. While the substantial criteria in the draft AML IP Guideline appears closer to the EU approach compared to the much broader essential facility provision in the draft IP Enforcement Regulation, both of them are divergent, to varying degrees, with EU's 'exceptional circumstances test' in many respects. This thesis proposes firstly that the IP Enforcement Regulation should set the tone for the IP Guideline. As to the substantial criteria within the IP Enforcement Regulation on refusal to license, it is recommended that Article 7 should be revised to contain two parts: a general principle and the exceptional circumstances to establish abusive refusals. Moreover, excessive pricing and FRAND-related provisions within the legal instruments and practice in China, *inter alia* the recent *Huawei/IDC* case, have been reviewed, demonstrating that in this respect China generally takes an EU-like position. A final remark in this chapter relates to the institutional reform in China. After finding that merging the three competition law enforcement authorities into one single, independent EU Commission-like enforcement authority is not feasible in the foreseeable future, this thesis proposes to pursue the second best – merging the two competition law divisions under the NDRC and the SAIC into one agency in charge of non-merger cases. If it is unlikely to set one

new independent agency by incorporating the two competition law divisions under the NDRC and the SAIC, merging the competition law function of one authority into the other should be otherwise pursued. If it is the case, it is strongly recommended by this research that NDRC's competition law team should be merged into the SAIC's considering their different roles played in the state and the possible effects caused thereof upon competition cases.



## CONCLUSION

This thesis examines the EU approaches on dominant undertaking's refusal to license intellectual property rights and follow-on pricing issue, and whether and to what extent the EU model could contribute to China's anti-monopoly practice. Striking a proper balance between unilateral exercise of intellectual property rights and competition rules is not an easy exercise. Even in the EU the CJEU could only touch upon the relationship between these two instruments on a case-by-case basis. This difficulty is further enhanced in China by the fact that the newly emerging competition law jurisdiction apparently has not, through its competition law enforcement activities, accumulated sufficient experience in merely six years. Moreover, in the absence of an analytical framework tailored for specific practices of intellectual property right owners, one may raise the concern that industrial policy considerations would be given a superior position by the competition law authorities and prevail over competition policy considerations in individual cases.<sup>1</sup> Thus, it might be safe to conclude that it is necessary for Chinese lawmakers to learn successful international experience in order to examine whether specific unilateral exercise of intellectual property rights by right owners, such as the behaviour of refusal to license, is abusive or not.

Throughout the chapter 1, significant commonalities between the EU and China's competition law were examined at length.<sup>2</sup> The analysis demonstrated that the major components of the Anti-Monopoly Law ('AML') text are modelled after EU competition law rather than the US antitrust rules. The multiple objectives pursued by the AML<sup>3</sup> have been observed to be similar to those in the EU, or the US antitrust policies prior to the Chicago School,<sup>4</sup> making foreign investors feel like in an EU-like legal environment which they are familiar with.<sup>5</sup> It is the EU competition law that has influenced most aspects of the three competition law realms of anticompetitive agreements, abuse of dominance and merger review. Taking abuse of dominance for an example, the analysis has observed that the AML has adopted an EU-like model, including the most significant factors in reviewing abusive cases, for instance the

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<sup>1</sup> See *supra* chapter 1, section 2.1.

<sup>2</sup> See *supra* chapter 1, section 2.

<sup>3</sup> See *supra* chapter 1, section 2.1.

<sup>4</sup> See Thomas R. Howell, Alan Wm. Wolff, Rachel Howe and Diane Oh, 'China's New Anti-Monopoly Law: A Perspective from the United States' (2009) 18 *Pacific Rim Law & Policy Journal* 53, p63.

<sup>5</sup> See Maher M Dabbah, 'The Development of Sound Competition Law and Policy in China: An (Im)possible Dream', (2007) 30(2) *World Competition* 341, p355.

definition of relevant market, the concept of a dominant market position, the relevant aspects in assessing a dominance position, specific prohibited abusive practices.<sup>6</sup> Apart from the substantial provisions, the enforcement regime of Chinese competition law was found to be also influenced by the EU administrative agency-oriented model due to China's civil law tradition.<sup>7</sup> Given the backdrop of the increasingly close EU-China relationship with respect to competition law,<sup>8</sup> it is highly likely that the EU successful experience, *inter alia* in certain complicated competition issues such as those at the intersection of competition law and IPR, could provide further guidance for China.

Building on this conclusion, the attention in chapter 2 and 3 then turned to the analysis of the EU approach on refusal to license, and more particularly to the development and definition of the 'exceptional circumstances test'. Faced with the fundamental question of how the competition rules should be set towards right owners' unilateral refusal to license behaviour, the CJEU developed the 'exceptional circumstances test' to deal with this matter. The CJEU in *Magill* established the main principle in refusal to license IPR cases that "the exercise of an exclusive right by the proprietor may, in exceptional circumstances, involve abusive conduct".<sup>9</sup> The EU Commission and Courts however have been at pains in the following cases, including *IMS Health* and *Microsoft I*, to interpret the content of the 'exceptional circumstances test', namely the three prongs of exceptional circumstances and one prong of justification, in order to improve the legal certainty of the analytical framework for the competition authorities and courts at Member States' level and the competition law practitioners.

With regard to the indispensability condition, the EU case law requires that it should not only be undisputed that there is no other available substitutes, even though they may be disadvantageous, but it should also be demonstrated that there are "technical, legal or even economic obstacles capable of making it impossible, or even unreasonably difficult, for any other undertaking alone or in cooperation to potentially establish a substitute".<sup>10</sup> The indispensability condition, as other two exceptional circumstances in the 'exceptional circumstances test' – elimination of the competition on the downstream market, and novelty of a new/innovative product – is a question of degree, to a certain extent depending on how to interpret the new product condition: if the new product condition is narrowly interpreted as in

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<sup>6</sup> See *supra* chapter 1, section 2.2.2.

<sup>7</sup> See *supra* chapter 1, section 3.1.

<sup>8</sup> See *supra* chapter 1, section 4.

<sup>9</sup> Judgment in *Magill*, C-241/91 P and C-242/91 P, ECLI:EU:C:1995:98, Para 50.

<sup>10</sup> Judgment in *Oscar Bronner*, C-7/97, ECLI:EU:C:1998:264, Para 43 and 44.

*Magill* and *IMS Health*, consequently a higher standard of indispensability shall be applied; if the new product condition is extensively interpreted in the sense that a more attractive product with improvements in certain features is sufficient as in *Microsoft I*, indispensability condition would be fulfilled if the input could increase the appeal of the competitors' (proposed) products and failure to supply the input would place the competitors at a disadvantage.<sup>11</sup>

Regarding the elimination of competition condition, it is argued to have the same effect as the condition of indispensability while these two conditions have slight difference on their focuses.<sup>12</sup> If an IPR protected input produced on the upstream market has been acknowledged to be indispensable for the production on the downstream market, refusal to grant a license to access to such intellectual property would likely lead to the exclusion of its competitors once the right owner intends to leave himself the downstream market. Therefore, fulfilment of one requirement normally results in the attainment of the other one. An obvious difference between *Microsoft I* case and the experience of EU Commission and Court of Justice in previous cases lies in that, either in *Magill* or in *IMS Health* all the effective competition on the downstream market was immediately – instantly or in no longer than a few days – eliminated once the competitors were refused to access to the copyright. The General Court in *Microsoft I* ruled that it is not necessary to wait until there is no more competition left on the market, and the different terminologies used by the EU Commission – *risk of elimination of competition* and *likely to eliminate competition* – have nothing to do with the standard of assessment for this condition.<sup>13</sup> A likely prediction about the eliminative effect on competition over time would suffice for the competition authorities. It would be too late to restore the competition process if the infringement has not been brought to an end until the completion of elimination of all the competition. The harm to the competition process and the consumers may be irreparable if it is obliged to prove the actual outcomes. Furthermore, that elimination of all competition, according to the General Court, does not imply that there are no other participants on the market. The existence of several *de minimis* players, who could not be seen as viable competitive constraints, cannot refute the conclusion that all effective competition is at risk of being eliminated on the market.<sup>14</sup>

As to the new product condition, the CJEU held in *IMS Health* that “the refusal [...] may be

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<sup>11</sup> See Thomas Eilmansberger, ‘The Essential Facilities Doctrine under Art. 82: What is the State of Affairs after *IMS Health* and *Microsoft*?’ (2005) 16 *King's College Law Journal* 329, p339.

<sup>12</sup> See *supra* chapter 3, section 2.2.

<sup>13</sup> Judgment of 17 September 2007, *Microsoft v Commission*, T-201/04, ECR, ECLI: EU: T: 2007: 289, Para 561.

<sup>14</sup> *ibid*, Para 593.

regarded as abusive only where the undertaking which requested the licence does not intend to limit itself essentially to duplicating the goods or services already offered on the secondary market by the owner of the intellectual property right, but *intends to produce new goods or services not offered by the owner of the right and for which there is a potential consumer demand.*”<sup>15</sup> The new product condition is considered as a bad proxy to assess the anti-competitive effect on the relevant market caused by the refusal at issue since newness is a variable which is difficult to define and quantify in the framework of competition law.<sup>16</sup> It is not clear how much degree of innovation represented in a product is required to make it a new product under Article 102 TFEU. In addition, there are divergent opinions on whether this condition requires a new product to compete with existing products on the same market.

The unclear interpretation of new product condition has become even more complicated since the General Court in *Microsoft I* added follow-on innovation into the ‘exceptional circumstances test’ and replaced the new product condition by a broader notion of *consumer harm*.<sup>17</sup> The General Court in *Microsoft I* considered that the conditions in the ‘exceptional circumstances test’ were not exhaustive, asserting that the prevention of the appearance of a new product in refusal to license cases might merely be one *example* of possible criteria to determine whether the refusal may cause disadvantages for the customers. The General Court maintained that Article 102 TFEU would be infringed not only by practices which prejudice consumers directly, but also by those which indirectly harm their interests.<sup>18</sup> Thus a limitation on technical development of the entire industry deriving from the dominant undertaking’s refusal is also within the meaning of Article 102 TFEU. The broader interpretation of the General Court in *Microsoft I* may be due to the facts that: (1) defining precisely the threshold of being a new product is problematic in practice; (2) Microsoft disrupted prior levels of supply and entered into the workgroup server system market, rather than refused to start to supply, which gave rise to that (3) the rivals were not capable of demonstrating their ability to create new products with breakthrough innovations but merely being able to provide value-added competition on the basis of product quality if the interoperability information could be accessed; (4) the characteristic of interoperability information determines that the products offered by the competitors directly compete with the product offered by Microsoft.

The original interpretation of the new product condition imposes a higher standard burden of

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<sup>15</sup> Judgment in *IMS Health*, C-418/01, ECLI: EU: C: 2004: 257, Para 49. (emphasis added)

<sup>16</sup> See *supra* chapter 3, section 2.3.1.

<sup>17</sup> Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 643-665.

<sup>18</sup> *Ibid*, Para 664.

proof on the competition authorities, aiming to protect the legitimate exercise of IPR held by a dominant undertaking so as to reward its previous innovatory efforts. It requires proof of novelty of the new product and evidence of unmet consumer demand, making the refusal behaviour abusive only in exceptional situations. Nevertheless, the practical difficulty of such an interpretation has given way to the extensive interpretation of the new product condition. The extensive interpretation is based on the belief that consumer welfare is the ultimate objective and it would be better served by protecting competition for innovations, especially in the dynamically competitive industries. According to the follow-on innovation approach, it is sufficient for the competitors to demonstrate their “intellectual and financial resources to develop the market in some way”<sup>19</sup> and some “degree of novelty of a product which the competitor was not yet in a position to produce”.<sup>20</sup> It might be even not necessary to define the proposed product in detail which the technology development would bring about.<sup>21</sup> If the technology development is very likely once the essential IPR were accessible for the requesting rivals, the right owner may not be able to unilaterally turn down the request. Then this test would be apparently satisfied in almost every IPR case – it goes without saying that the essential technology information disclosed from a dominant undertaking on the market would be valuable for its competitors, directly or indirectly, to improve their competing products.<sup>22</sup> The judgment of the *Microsoft I* case implies that the right to refuse would thus become an exception rather than a rule.<sup>23</sup> Thus the right to refuse to grant a license could be claimed only when the requesting parties’ intention to develop the market would be highly unlikely achieved.<sup>24</sup> Consequently, in the long run both the entire industry and the consumer welfare would be impaired. Yet, the cases involving copyrights may be relatively less affected by this lower standard than patent cases, since the indispensability condition is difficult to pass in cases

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<sup>19</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

<sup>20</sup> John Temple Lang, ‘Mandating access: the principles and the problems in Intellectual Property and competition policy’, (2004) 15(5) *European Business Law Review* 1087, p1111.

<sup>21</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123; Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p902.

<sup>22</sup> See e.g. James Killick, ‘*IMS* and *Microsoft* Judged in the Cold Light of *IMS*’ (2004) 1(2) *The Competition Law Review* 23, p43; Christian Ahlborn and David S. Evans, ‘The Microsoft Judgment and Its Implications for Competition Policy Towards Dominant Firms in Europe’ (2009) 75 *Antitrust Law Journal* 887, p914.

<sup>23</sup> See Ian S. Forrester, ‘Magill Revisited’, in Inge Govaere, Reinhard Quick and Marco Bronckers (eds.), *Trade and Competition Law in the EU and Beyond* (Edward Elgar, 2011) 376, p388: “In less than 20 years, we have moved from anything being surprising (*Magill*) to everything being possible (*Microsoft*).” See also Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

<sup>24</sup> Ekaterina Rousseva, *Rethinking Exclusionary Abuses in EU Competition Law* (Hart Publishing, 2010), p123.

involving copyrights.<sup>25</sup>

The EU *Microsoft I* case, as a milestone exclusionary case under the framework of Article 102 TFEU, has provided the EU Commission and General Court a good opportunity to re-consider the application of the ‘exceptional circumstances test’ in the fast-moving industries and more detailed meaning of each condition. After having adopted lower criteria of the ‘exceptional circumstances test’, the EU Commission (and the General Court as well) has demonstrated its interventionist stance towards the refusal behaviour by an undertaking with a dominant position in a market characterized by strong network effects. This stance is even more obvious when compared to the US antitrust authorities’ generally lenient approach on unconditional, unilateral refusal to license.

While the EU Commission and EU courts have taken their roles in formulating the EU criteria, the thesis investigated in chapter 5 whether the EU approach could be transplanted, or is being considered by Chinese lawmakers. After investigating the state-of-the-art understanding of Chinese courts on the relevant market definition and dominant position assessment in dynamically competitive industries, the case study of *Qihoo/Tencent*<sup>26</sup> has shed some light particularly on the definition of relevant product and geographic market in software industry against the scant judicial experience since the enactment of the AML in China. Also, the unique economic features and profit mode of the IM market have been taken into consideration by the first instance court and China’s Supreme Court in assessing the market power. Prior to the adoption of any AML guidance in the IP context, this case has demonstrated Chinese courts’ confirmative answer to the *pre-question* – whether in abuse cases involving IPRs the prohibitions of the AML are only applied to activities conducted by undertakings with a dominant position. Definitely the possession of a dominant position is a premise even in such fast growing sectors before assessing allegedly abusive conduct’s effect on competition. Though in some parts of the judgments the courts came to the conclusions without convincing reasoning, this case still represents the Chinese courts’ state-of-the-art understanding as to how the competition rules should be applied in a more economic way in dynamically competitive industries. More importantly, it is the *first* Chinese competition case where some observations made by the EU Commission in an EU competition law case have been used by the parties to

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<sup>25</sup> Christian Ahlborn, Vincenzo Denicolò, Damien Geradin and A Jorge Padilla, ‘DG Comp’s Discussion Paper on Article 82: Implications of the proposed Framework and Antitrust Rules for Dynamically Competitive Industries’, available at <http://ec.europa.eu/competition/antitrust/art82/057.pdf>, last visited on 20 July 2014, pp.47-48.

<sup>26</sup> See *supra* chapter 5, section 3.

support their viewpoints, and then been confirmed and quoted by a Chinese court in its judgment.

While the only IP-related provision within the AML (Article 55) leaves the question unanswered as to whether and under what conditions right owners' refusal to license behaviour would be treated as abuse of dominant position,<sup>27</sup> chapter 5 examined in details the envisaged substantial criteria on refusal to license within the draft *AML IP Guideline*<sup>28</sup> and the draft *IP Enforcement Regulation*<sup>29</sup>. It could be observed that the Chinese lawmakers have in the latest draft of *IP Enforcement Regulation* adopted a *lower* standard to establish an abusive refusal to license. The substantial conditions in the draft *AML IP Guideline* and the draft *IP Enforcement Regulation* could be labelled, in an EU-like way, as the indispensability condition, the elimination of competition condition, and the impact on the consumers/IPR holder condition. In the first place, while the conditions in the draft Guideline are apparently cumulative, the manner adopted in the draft Regulation makes it unclear whether the conditions are cumulative or alternative. And it is also vague whether the factors to be considered in the draft Regulation are close-ended like the draft Guideline, or the list is open-ended and the SAIC thus is entitled to take other relevant factors into consideration. In the second place, concerning the indispensability condition, in addition to the requirement in both documents that the IPR at issue is indispensable for other undertakings (including the requesting party) to effectively compete in the relevant market, the draft Regulation demands that within the market there should be no *reasonable* substitutions to the IPR at issue.<sup>30</sup> There is no further guidance on the standard the AML enforcement authority will employ to determine whether another IPR in the relevant market constitutes a *reasonable* substitution to the IPR held by the dominant undertaking. If the enforcement authority adopts a high standard to define the concept

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<sup>27</sup> See *supra* chapter 5, section 2.2.

<sup>28</sup> *Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights*. The fifth draft AML IP Guideline was released in the International Symposium of Forefront Issues of Anti-Monopoly Law Enforcement on 14 August 2012. An unofficial English translation is available as an appendix to the Joint Comments of the American Bar Association Section of Antitrust Law, Section of Intellectual Property Law and Section of International Law on the SAIC Draft Guide on Anti-Monopoly Law Enforcement in the Field of Intellectual Property Rights, available at [http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments\\_finalpackage.pdf](http://chinaipr2.files.wordpress.com/2012/10/aba-china-aml-ip-guidelines-comments_finalpackage.pdf), last visited on 29 January 2014, more analysis of relevant provisions of the Guideline see *infra* chapter 5, section 4.1.

<sup>29</sup> To implement the AML, the State of Administration for Industry & Commerce ('SAIC') has drafted the *Implementing Rules on the Prohibition of Abuses of Intellectual Property Rights for Purposes of Eliminating or Restricting Competition* and published the draft for comment on 10 June 2014, available at [http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610\\_145803.html](http://www.saic.gov.cn/gzhd/zqyj/201406/t20140610_145803.html), last visited on 20 July 2014, more analysis of relevant provisions of the Regulation see *infra* chapter 5, section 4.2.

<sup>30</sup> *Ibid*, Article 7, Para 2.

‘reasonable substitution’, the consequence will be that some less competitive IPRs will be ignored and it will result in a lower standard to find the IPR at issue as an essential facility for other undertakings. In the third place, as to the elimination of competition condition, the approach of the draft Regulation requires the anti-competitive effects caused by such refusal on the competition *or* the innovation in the market,<sup>31</sup> while the approach of the draft Guideline demands that the refusal to license should cause negative effects on both of the competition *and* the innovation in the relevant market.<sup>32</sup> Apparently the standard of the draft Regulation is lower since this requirement is satisfied as long as the enforcement authority identifies negative effects either on market competition or on the innovative activities. In the fourth place, the draft Guideline and the draft Regulation have divergent criteria with respect to the impacts on the consumers/IPR holder condition. Whereas the draft Guideline requires that there should be unmet consumer demands due to the refusal conduct<sup>33</sup> which is consistent with the EU practice, the draft Regulation attaches importance to whether the obligation to license would potentially cause unreasonable harm on the right holder.<sup>34</sup> Compared to the consumer welfare condition, from the perspective of the enforcement authority it might be a relatively simple task to prove the non-existence of potentially unreasonable harm on the IPR holder to establish an abusive refusal to license. What is more, the standard in interpreting the term ‘unreasonable harm’ is at the discretion of the enforcement authority.

Taking the dissimilarities between the draft Guideline and the draft Regulation into consideration, it might be possible that quite divergent conclusions could be reached by the SAIC in the China’s Microsoft interoperability information disclosure case depending on which criteria the enforcement authority would like to apply. While by the criteria set by the draft Regulation Microsoft’s refusal to disclose information is highly likely to be treated as abuse of dominance, the software firm will have more chance to exempt from competition law liability if the authority examines its practice against the criteria of the Guideline even the interoperability information is considered to be *de facto* essential facility in the relevant market. Admittedly, this is based on the assumption that both of the envisaged criteria on refusal to license within the draft Guideline and the draft Regulation become effective which the enforcement authority could apply. Therefore, when the Guideline and the Regulation come into effect will be significant for SAIC’s investigation on Microsoft. Considering the aforementioned fact that it is still unknown when the drafting of the AML IP Guideline will be resumed, for Microsoft

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<sup>31</sup> Ibid.

<sup>32</sup> The AML IP Guideline (fifth draft), *supra* note 28, Article 17, Para 2(2).

<sup>33</sup> Ibid.

<sup>34</sup> The IP Enforcement Regulation (draft for comment), *supra* note 29, Article 7, Para 2.



investigation there may be two possibilities. Either, the draft Regulation remains unchanged in essence and becomes effective sooner than the SAIC delivers its final decision. If this is the case, Microsoft may become the first offender of the Article 7 of the IP Enforcement Regulation. Or, if the SAIC issues its final decision before the effective date of the IP Enforcement Regulation, it is completely unclear as to how the SAIC will interpret the essential facility doctrine to distinguish abusive refusal behaviour from right owners' lawful exercise of intellectual property rights.

On the one hand, the substantial criteria proposed in the draft *AML IP Guideline* appears closer to the EU approach compared to the much broader essential facility provision provided in the draft *IP Enforcement Regulation*. Firstly, like what has been confirmed by EU courts in a number of cases,<sup>35</sup> the provision within the draft Guideline provides a similar general principle that it is at the discretion of the right holder to license, or otherwise to refuse to license, its IPR to a third party, including its competitors, making abusive refusal to license only in exceptional cases. Secondly, compared to the provision in draft Regulation, the way the provision in the draft Guideline structures the substantial conditions explicitly demonstrates that the three conditions are cumulative, which is akin to the CJEU's position in *IMS Health* case.<sup>36</sup> Thirdly, like EU's 'exceptional circumstances test', in order to establish an exceptional abusive refusal to license the provision in the draft Guideline also takes into account the indispensability of the IPR requested, the impacts brought about by the refusal on market competition and innovation, and the existence of unmet consumer demand.

On the other hand, both of the draft *AML IP Guideline* and the draft *IP Enforcement Regulation* are divergent, to varying degrees, with EU's 'exceptional circumstances test' in many respects. First of all, there is no 'upstream-downstream markets' requirement either in the draft Guideline or in the draft Regulation, thus remaining the question open as to whether companies in China could force a dominant competitor at the same market level to license essential IPR and compete directly against the licensor. More importantly, unlike the three cumulative conditions in the 'exceptional circumstances test' that the CJEU has carefully established to confine abusive refusal to license to exceptional situations, the vague conditions, either in the draft Guideline or in the draft Regulation, provide the enforcement authority too

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<sup>35</sup> E.g. Judgment in *Volvo*, 238/87, ECLI:EU:C:1988:477, Para 7-8; Judgment in *Magill* ECLI:EU:C:1995:98, Para. 49; Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para. 34; Judgment in *Microsoft v Commission*, ECLI: EU: T: 2007: 289, Para 331.

<sup>36</sup> Judgment in *IMS Health* ECLI: EU: C: 2004: 257, Para 38 and Para 52.

much discretion, making it possible that these conditions might be interpreted in such a broad manner that refusal to license IPR is prohibited as a rule rather than an exception.<sup>37</sup>

This thesis thus proposes firstly that the *IP Enforcement Regulation* should set the tone for the *AML IP Guideline* owing to their different roles in the competition law system.<sup>38</sup> As to the substantial criteria within the *IP Enforcement Regulation* on refusal to license, this thesis recommended revising Article 7 to contain two parts: a general principle and the exceptional circumstances to establish abusive refusals. To safeguard the legitimate interests of IPR holders, a general principle like the starting point of the EU competition law (and that in the current draft *AML IP Guideline*) should be stated that, in normal circumstances any IPR holders, whether dominant or not, should have the right to choose its trading partners and the AML enforcement authorities will not impose upon the IPR holders an obligation to license their IPRs. Then, it is vital to revise current essential facility provision in the draft *IP Enforcement Regulation* into the EU-like exceptional circumstances. It should be noted that there have been two standards in the EU case law. Compared to the stringent criteria established by the CJEU in *Magill* and *IMS Health*, the exceptional circumstances test interpreted by the General Court in *Microsoft I* could chill the innovators and thus be criticized.<sup>39</sup> Considering that the current criteria set up in the draft Regulation is even broader than the General Court's *Microsoft I* standard, the desired target EU template should be the *Magill/IMS Health* standard. Considering that it is unlikely that the *IP Enforcement Regulation* would completely copy the strict criteria set out in *IMS Health*, it may be realistic to re-set the Chinese version of competition criteria on refusal to license in between the EU *Magill/IMS Health* standard and the *Microsoft I* standard. The second part was suggested to be re-structured as follows:

Absent due justifications, a refusal to license intellectual property rights would be treated by the enforcement authority as abusive only in exceptional circumstances where the following three conditions are cumulatively met:

- (1) The IPR at issue is indispensable for carrying on a particular business on the downstream market;
- (2) The refusal will eliminate all effective competition on the downstream market;
- (3) The refusal is likely to lead to consumer harm.

Such revision would bring current Article 7 of the draft *IP Enforcement Regulation* closer to the EU practice and enhance legal certainty for one thing. For another, such proposed

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<sup>37</sup> See *supra* chapter 5, section 4.3.

<sup>38</sup> See *supra* chapter 5, at page 239.

<sup>39</sup> See *supra* chapter 3, section 2.5.

framework also leaves room for the Chinese enforcement authority to use its discretion to employ appropriate standard in a given case. As to the potential *AML IP Guideline*, based on the criteria set out in the *IP Enforcement Regulation*, more detailed guidance on assessing refusal to license conduct could be provided. The *AML IP Guideline*, after obtaining experience from enforcement authority's activities, could summarize the standards that have been adopted by the authority.

On top of the substantial criteria established from the perspective of competition towards unilateral refusal to license behaviour, it was found in chapter 4 that royalty setting issue, as a follow-on matter, could also be related to refusal to license. The analysis distinguished two situations where the concept FRAND could be related to IPR holder's refusal to license in non-SEP cases and SEP cases. The EU Commission in *Motorola FRAND* case<sup>40</sup> found that the standardisation context and Motorola's FRAND commitment constitute 'exceptional circumstances', thus distinguishing this case from other cases where the general principle that a patent holder has the right to refuse to license could apply. In light of the anti-competitive effects brought about by Motorola's seeking and enforcement of an SEP-based injunction, the abusive practice in this case could be clearly distinguished from the unconditional refusal to license behaviour (the main subject of this research), the main purpose of which is to exclude competitors from the market. In this case, it seems Motorola's refusal to license behaviour is merely a means in negotiation to threaten the standard implementers to conclude the licensing agreements in favour of the SEP holder. In the EU neither situation has provided a meaningful definition of FRAND. Moreover, the two-step approach established in *United Brands* is also unworkable in assessing whether a high price is unfair when intellectual property is involved. At the EU level the fact remains that neither the EU Commission nor the EU courts have formulated a predictable approach that allows the IPR holders to evaluate whether their royalty rates comply with the FRAND requirement. Chapter 5 reviewed the excessive pricing and FRAND-related provisions within the legal instruments and practice in China, *inter alia* the recent *Huawei/IDC* case, demonstrating that in this respect China generally takes an EU-like position. To strike a balance between maintaining competitive market order and providing sufficient compensation for IPR holders, economists have, from different angles, proposed several models, by which the economic value of the IPR at issue could be indirectly calculated and thus a FRAND royalty rate could be determined.<sup>41</sup> However, even the economic discussion on FRAND royalties remains somewhat limited helpful since the

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<sup>40</sup> See *supra* chapter 4, section 2.

<sup>41</sup> See *supra* chapter 4, section 3.

“abstract and simplified” models leave many issues open in the real markets.<sup>42</sup> The limitation is particularly obvious in the licensing scenario following an abusive refusal to license ruling.

Throughout the thesis, the analytical framework on refusal to license and its follow-on royalty rate setting issue were highlighted and examined in detail. Apart from the substantial criteria, a more consistent and coherent enforcement regime is a commendable strategy to implement these competition rules. Based on the comprehensive AML, China has established a two-layer, three-pronged enforcement regime.<sup>43</sup> This EU-like administrative-oriented enforcement regime has adopted sets of procedural and substantial rules to implement the law. Hence, a final remark in this thesis relates to the institutional reform in China, with the aim of overcoming the problems within the current enforcement regime (including inter-authority and intra-authority problems)<sup>44</sup>. After finding that merging the three competition law enforcement authorities into one single, independent EU Commission-like enforcement authority is not feasible in the foreseeable future, this thesis proposed to pursue the second best – merging the two competition law divisions under the NDRC and the SAIC into one agency in charge of non-merger cases.

Such institutional design might be, in the first place, reasonable in terms of the types of competition law cases. While the difference between merger cases and non-merger cases is more visible, assigning price-related cases and non price-related cases to two agencies is more or less artificial. Such reform might be, in the second place, reasonable in terms of the roles played by the enforcement authorities. While the MOFCOM provides *ex ante* control, both of the NDRC and the SAIC examine agreements that are already concluded or dominant undertakings’ conducts that are already taken. Also such reform would not fundamentally alter the resource distribution for all three authorities. Thirdly, such design might be reasonable in terms of the establishment of a well-structured competition law legislation system. Such reform does not require any modification of the AML provisions, but also could facilitate drafting of AML implementing rules and guidelines for non-merger competition issues. This advantage would be obvious in drafting the AML IP Guideline as well as the IP Enforcement Regulation. Fourthly, examination of the refusal to license conduct could benefit particularly from the merge of competition law divisions under the NDRC and the SAIC, since in that case not only the refusal behaviour itself but also the follow-on royalty rate setting issue could be scrutinized

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<sup>42</sup> See Mikko Valimäki, “A Flexible Approach to RAND Licensing”, (2008) 28(12) *European Competition Law Review* 686, p689.

<sup>43</sup> See *supra* chapter 1, section 3.1.

<sup>44</sup> See *supra* chapter 1, section 3.2 and 3.3.

by the same agency.

Lastly, if it is unlikely to set one new independent agency by incorporating the two competition law divisions under the NDRC and the SAIC, merging the competition law function of one authority into the other should be otherwise pursued. If it is the case, it was strongly recommended by this research that NDRC's competition law team should be merged into the SAIC's considering their different roles played in the state and the possible effects caused thereof upon competition cases.

To sum up, in examining the main question as to whether and to what extent the EU approach on refusal to license intellectual property rights could be transposed to China, the research has demonstrated that in general Chinese competition law has, in many respects, modelled after the EU competition rules. With particular regard to the refusal to license issue, it might be safe to conclude that the Chinese lawmakers are also likely to adopt EU-like criteria in this respect, but not the more lenient US approach. Yet, the analysis demonstrated that the proposed criteria within the draft *AML IP Guideline* and the draft *IP Enforcement Regulation* towards refusal to license is such a case where, rather than entirely copying the EU approach, Chinese lawmakers appear to import from the EU practice by picking and choosing from EU competition law norms. In light of the foregoing analysis, this thesis suggests to revise the envisaged essential facility provision on refusal to license, which is currently in drafting progress in China, into the stricter criteria which should be located in between the EU *Magill/IMS Health* standard and the *Microsoft I* standard considering that the former standard is currently not realistic.



# APPENDIX

Unofficial Translation

## **Anti-Monopoly Law of the People's Republic of China**

(Adopted by the 29th Session of the Standing Committee of the 10th National People's Congress on August 30, 2007)

### **Chapter One General Provisions**

#### **Article 1**

This law is enacted for the purposes of preventing and prohibiting Monopolistic Conduct, protecting fair market competition, promoting efficiency of economic operation, safeguarding the interests of consumers and the public interests, and promoting the healthy development of the socialist market economy.

#### **Article 2**

This law is applicable to Monopolistic Conduct in economic activities within the territory of the People's Republic of China. This law is applicable to Monopolistic Conduct outside the territory of the People's Republic of China that has eliminative or restrictive effects on competition in the domestic market of the People's Republic of China.

#### **Article 3**

"Monopolistic Conduct" referred to herein includes:

- (1) conclusion of monopoly agreements by undertakings;
- (2) abuse of dominant market positions by undertakings;
- (3) concentrations of undertakings that have or are likely to have the effect of eliminating or restricting competition.

#### **Article 4**

The State shall formulate and implement competition rules suitable for the socialist market economy to improve control of the macro-economy and to strengthen a unified, open, competitive, and orderly market system.

#### **Article 5**

Undertakings may implement concentrations in accordance with the law through fair competition and voluntary combination to expand their business scale and to improve their market competitiveness.

#### **Article 6**

Undertakings with dominant market positions shall not abuse their dominant market positions to eliminate or restrict competition.

#### **Article 7**

With respect to industries that are controlled by the state-owned economy and that are critical to the wellbeing of the national economy and national security, as well as industries in which exclusive operation and exclusive sales are the norm of business in accordance with the law, the State shall protect the lawful business activities of the undertakings in such industries. The State shall regulate and supervise the business activities of such undertakings and regulate the prices of commodities and services provided by such undertakings in accordance with the law so as to protect the interests of the consumers and to promote technological progress.

Undertakings in the industries referred to in the preceding paragraph shall conduct their business in accordance with the law, shall be honest and reputable in their business dealings, and shall maintain strict self-discipline and accept public supervision. They shall not harm the interests of consumers by utilizing their controlling positions or their status as the exclusive provider of certain services or products.

#### **Article 8**

Administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs shall not abuse their administrative power to eliminate or restrict competition.

#### **Article 9**

The State Council shall establish the Anti-Monopoly Commission which shall be responsible for organizing, coordinating, and guiding the anti-monopoly work. The Anti-Monopoly Commission shall perform the following duties:

- (1) to research and formulate competition policies;
- (2) to organize investigations, assess the overall market competition conditions, and



publish the assessment reports;

- (3) to formulate and promulgate anti-monopoly guidelines;
- (4) to coordinate the anti-monopoly administrative enforcement work;
- (5) to undertake other duties as designated by the State Council.

#### **Article 10**

The authority appointed by the State Council to perform the function of anti-monopoly law enforcement (the “Anti-Monopoly Law Enforcement Authority under the State Council”) shall be responsible for the anti-monopoly law enforcement work in accordance with the provisions of this law.

The Anti-Monopoly Law Enforcement Authority under the State Council may, if there is a practical need to do so, delegate to the corresponding agencies of the People’s Governments at the levels of province, autonomous region and municipality directly under the central government responsibilities of the anti-monopoly law enforcement work in accordance with the provisions of this law, if necessary.

#### **Article 11**

The trade associations shall strengthen the self-discipline of industries to lead undertakings within their respective industries to carry out lawful competition and to maintain the order of market competition.

#### **Article 12**

“Undertakings” referred to herein mean natural persons, legal persons and other organizations that are engaged in manufacturing or otherwise dealing with commodities, or providing services.

“Relevant Market” referred to herein means the scope of commodities and the scope of territory within which the undertakings compete with each other during a specific period of time with respect to specific commodities or services (collectively “commodities”).

### **Chapter Two Monopoly Agreements**

#### **Article 13**

The following Monopoly Agreements among undertakings with competing relationship shall be prohibited:

- (1) fixing or changing the price of commodities;
- (2) limiting the outputs or sales volume of commodities;

- (3) allocating the sales markets or the raw material purchasing markets;
- (4) restricting the purchase of new technology or new equipment or restricting the development of new products;
- (5) jointly boycotting transactions; or
- (6) other Monopoly Agreements determined by the Anti-Monopoly Law Enforcement Authority under the State Council.

“Monopoly Agreements” referred to herein mean agreements, decisions or other concerted conducts that eliminate or restrict competition.

#### **Article 14**

Undertakings are prohibited from entering into Monopoly Agreements with their counter-parties that:

- (1) fix the resale price of commodities sold to third parties;
- (2) limit the minimum resale price of commodities sold to third parties; or
- (3) other Monopoly Agreements determined by the Anti-Monopoly Law Enforcement Authority under the State Council.

#### **Article 15**

The provisions of Articles 13 and 14 shall not apply to agreements among undertakings if the undertakings can prove that such agreements fall under any of the following:

- (1) for the purpose of improving technology, researching and developing new products;
- (2) for the purpose of improving the product quality, reducing costs, enhancing efficiency, unifying specifications and standards of products, or implementing division of labor based on specialization;
- (3) for the purpose of improving operational efficiency of small and medium- sized undertakings and enhancing their competitiveness;
- (4) for the purpose of achieving public interests, including, but not limited to, energy saving, environmental protection, and disaster relief;
- (5) for the purpose of alleviating serious decreases in sales volume or distinctive production surpluses due to economic depression;
- (6) for the purpose of safeguarding legitimate interests in foreign trade and foreign economic cooperation;
- (7) other circumstances as stipulated by laws and by the State Council.

If any Monopoly Agreements fall into the circumstances set forth in sub-clauses (1) to (5) above so that the provisions of Articles 13 and 14 are not applicable, the relevant undertakings must also prove that the agreement so concluded will not materially restrict

competition in the Relevant Market and that the agreement can allow consumers to share the benefits generated therefrom.

#### **Article 16**

The trade associations shall not organize undertakings within their industries to engage in Monopolistic Conduct prohibited under this Chapter.

### **Chapter Three Abuse of Dominant Market Position**

#### **Article 17**

Undertakings with dominant market positions are prohibited from abusing their dominant market positions by engaging in the following activities:

- (1) selling commodities at unfair high prices or buying commodities at unfair low prices;
- (2) selling commodities at prices below cost without any justification;
- (3) refusing to transact with counter-parties with respect to a transaction without any justification;
- (4) restricting, without any justification, their counter-parties to transact with such undertakings exclusively or to transact with other parties designated by such undertakings exclusively;
- (5) engaging in tie-in sales of commodities or imposing other unreasonable conditions with respect to transactions without any justification;
- (6) applying differential treatments to counter-parties to transactions who have the same qualifications with respect to transaction price and other transaction terms, without any justification;
- (7) other activities that are deemed by the Anti-Monopoly Law Enforcement Authority of the State Council as abusing dominant market positions.

“Dominant Market Positions” referred to herein mean the market positions held by undertakings who are able to control the price or quantity of commodities, or other transaction terms in the Relevant Market or to block or affect the entry of other undertakings into the Relevant Market.

#### **Article 18**

A finding that certain undertaking has a Dominant Market Position shall be based on the following factors:

- (1) the market share of the undertaking in the Relevant Market, and the competition conditions in the Relevant Market;

- (2) the ability of the undertaking to control the sales market or the raw material purchasing market;
- (3) the financial resources and the technical capacities of the undertaking;
- (4) the extent to which other undertakings depend on the subject undertaking with respect to relevant transactions;
- (5) the level of difficulty for other undertakings to enter the Relevant Market;
- (6) other factors relating to the determination whether the subject undertaking has a Dominant Market Position.

#### **Article 19**

Undertakings may be presumed to have a Dominant Market Position if they satisfy any of the following conditions:

- (1) the market share of one undertaking in the Relevant Market accounts for 1/2;
  - (2) the joint market share of two undertakings in the Relevant Market accounts for 2/3;
- or
- (3) the joint market share of three undertakings in the Relevant Market accounts for 3/4.

In case of circumstances set forth in the sub-clauses (2) and (3) above, if any of such undertakings has a market share less than 1/10, it shall not be presumed to have a Dominant Market Position.

If an undertaking which is presumed to have a Dominant Market Position presents evidences showing otherwise, it shall not be deemed to have a Dominant Market Position.

### **Chapter Four Concentration of Undertakings**

#### **Article 20**

Concentration of undertakings means the following circumstances:

- (1) a merger of undertakings;
- (2) an acquisition by an undertaking of the control of other undertakings through acquiring equity or assets;
- (3) an undertaking, by contracts or other means, acquiring control of other undertakings or the capability to exercise decisive influence on other undertakings.

#### **Article 21**

If a concentration of undertakings meets the thresholds for notification as stipulated by the State Council, the relevant undertakings shall file a notification with the Anti-monopoly Law Enforcement Authority under the State Council in advance. Without filing such a

notification, the undertakings shall be prohibited from implementing the concentration.

## **Article 22**

Undertakings are permitted not to file any notification with the Anti- Monopoly Law Enforcement Authority under the State Council if their concentration meets any of the following conditions:

- (1) one undertaking participating in the concentration owns more than 50% of the voting shares or assets of each of the other participating undertakings;
- (2) more than 50% of the voting shares or assets of every undertaking participating in the concentration are owned by a single undertaking that does not participate in the concentration.

## **Article 23**

When undertakings file a notification of concentration with the Anti- Monopoly Law Enforcement Authority under the State Council, they shall submit the following documents and materials:

- (1) the notification;
- (2) an statement explaining the impact of the concentration upon the competition conditions of the Relevant Market;
- (3) the concentration agreement;
- (4) the financial and accounting reports of the undertakings participating in the concentration in the preceding fiscal year, which are audited by accountant firms;
- (5) other documents and materials required by the Anti-Monopoly Law Enforcement Authority under the State Council.

The notification shall indicate clearly the name, address and business scope of the undertakings participating in the concentration, the proposed date for implementing the concentration and other matters as stipulated by the Anti-Monopoly Law Enforcement Authority under the State Council.

## **Article 24**

If the documents and materials submitted by undertakings are not complete, undertakings shall file supplementary documents and materials within the time limit specified by the Anti-Monopoly Law Enforcement Authority under the State Council. If the undertakings make no supplementary filing within the specified time limit, it shall be deemed that no notification is filed.

## **Article 25**

The Anti-Monopoly Law Enforcement Authority under the State Council shall conduct a preliminary review of the reporting undertakings, decide on whether to initiate further review, and notify the undertakings in writing of its decision within 30 days from the date of receipt of the documents and materials submitted by the undertakings in accordance with Article 23 hereof. The undertakings shall not implement the concentration before the Anti-Monopoly Law Enforcement Authority under the State Council makes its decision.

The undertakings may implement the concentration if the Anti-monopoly Law Enforcement Authority under the State Council decides not to initiate further review or makes no decision within the time limit.

#### **Article 26**

If the Anti-monopoly Law Enforcement Authority under the State Council decides to initiate further review, it shall complete the review within 90 days from the date of the decision, decide whether to prohibit the concentration of the undertakings and notify the undertakings in writing thereof; in case of a decision to prohibit the concentration of undertakings, it shall explain its reasons. Undertakings shall not implement the concentration during the review period.

Under any of the following circumstances, the Anti-monopoly Law Enforcement Authority under the State Council may extend the time limit for the review set forth in the above paragraph by giving a written notice to the undertakings, provided that the extension shall not exceed 60 days at the maximum:

- (1) the undertakings agree to extend the time limit for the review;
- (2) the documents or materials submitted by the undertakings are inaccurate and need further verification; or
- (3) material changes have occurred with respect to relevant circumstances since the undertakings filed the notification.

If the Anti-monopoly Law Enforcement Authority under the State Council makes no decision within the time limit, the undertakings may implement the concentration.

#### **Article 27**

The following factors shall be taken into consideration in the review of the concentration by undertakings:

- (1) the market shares of undertakings participating in the concentration in the Relevant Market and their ability to control of the market;
- (2) the degree of concentration in the Relevant Market;
- (3) the effect that the concentration of undertakings may have on market access and

technological progress;

(4) the effect that the concentration of undertakings may have on consumers and other relevant undertakings;

(5) the effect that the concentration of undertakings may have on the development of the national economy;

(6) other factors affecting the market competition that the Anti-Monopoly Law Enforcement Authority under the State Council deems relevant shall be taken into consideration.

### **Article 28**

The Anti-Monopoly Law Enforcement Authority under the State Council shall make a decision to prohibit a concentration of undertakings if such concentration has or may have the effect of eliminating or restricting competition. However, the Anti-Monopoly Law Enforcement Authority under the State Council may decide not to prohibit a concentration if the undertakings can prove that the positive effects of such concentration on the competition obviously outweigh its negative effects or that the concentration is in the public interest.

### **Article 29**

If the Anti-Monopoly Law Enforcement Authority under the State Council does not prohibit the concentration of undertakings, it may decide to impose restrictive conditions to reduce the adverse effects the concentration may have on competition.

### **Article 30**

The Anti-Monopoly Law Enforcement Authority under the State Council shall publicize in a timely manner its decisions to prohibit the concentration of undertakings or to impose restrictive conditions on the concentration of undertakings.

### **Article 31**

If the merger with or acquisition of domestic enterprises by foreign investors or other forms of concentration involving foreign investors concerns national security, in addition to the review of concentration of undertakings in accordance with the provisions of this Law, it shall be examined for national security review in accordance with relevant regulations of the State.

## **Chapter Five Abuse of Administrative Power to Eliminate or Restrict Competition**

### **Article 32**

Administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs shall not abuse their administrative powers to require or require in a disguised form organizations or individuals to deal in, purchase or use the commodities supplied by the undertakings designated by them.

### **Article 33**

Administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs shall not abuse their administrative powers and take any of the following actions to hinder the free flow of commodities among different regions:

(1) to charge discriminatory fees under separate fee categories or at different rates, or fix discriminatory prices for commodities originated from other regions;

(2) to impose on commodities originated from other regions technical requirements or inspection standards different from those applied to similar local commodities, or cause commodities originated from other regions to be subject to discriminatory technical measures such as duplicate inspection or certification, so as to restrict the entry of commodities originated from other regions into the local markets;

(3) to implement special administrative licensing measures applicable only to commodities originated from other regions, so as to restrict the entry of commodities originated from other regions into the local markets;

(4) to set up checkpoints or take other measures to block the entry of commodities originated from other regions or the flow of local commodities out of the region;

(5) other actions that may impede the free flow of commodities among different regions.

### **Article 34**

Administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs shall not abuse their administrative powers to exclude or restrict the participation of undertakings from other regions in local bidding activities by means such as prescribing discriminatory qualification requirements or standards or by not publishing information according to law.

### **Article 35**

Administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs shall not abuse their administrative powers to exclude or restrict investment in their region or establishment of branches or subsidiaries in



their region by undertakings from other regions, by applying means such as treatment not equal to what local undertakings are entitled to.

#### **Article 36**

Administrative agencies and organizations empowered by laws and regulations to have the function of administrating public affairs shall not abuse their administrative powers to compel undertakings to engage in any Monopolistic Conduct set forth hereunder.

#### **Article 37**

Administrative agencies shall not abuse their administrative powers to make regulations that contain provisions eliminating or restricting competition.

### **Chapter Six Investigation of Suspected Monopolistic Conduct**

#### **Article 38**

The Anti-Monopoly Law Enforcement Authority shall investigate suspected Monopolistic Conducts in accordance with the law.

Any organization or individual shall have the right to report any suspected Monopolistic Conduct to the Anti-Monopoly Law Enforcement Authority. The Anti-Monopoly Law Enforcement Authority shall maintain the confidentiality for the reporting organization or individual.

The Anti-Monopoly Law Enforcement Authority shall conduct necessary investigation if the report is in writing and includes relevant facts and evidence.

#### **Article 39**

When conducting investigations of the suspected Monopolistic Conduct, the Anti-Monopoly Law Enforcement Authority may take the following measures:

- (1) entering into business premises of the undertaking being investigated or other relevant places for inspection;
- (2) questioning the undertakings being investigated, interested parties, and other relevant organizations or individuals, requesting them to clarify the relevant facts and circumstances;
- (3) examining or copying relevant documents, agreements, accounting books, business correspondence, electronic data and other materials of the undertakings being investigated, interested parties, and other relevant organizations or individuals;
- (4) sealing or seizing relevant evidence;
- (5) making inquiries about the bank accounts of the undertakings.

Measures as stipulated in the foregoing paragraph may be implemented only after a written report has been submitted to the principal responsible persons of the Anti-Monopoly Law Enforcement Authority and the relevant approval has been obtained.

#### **Article 40**

Investigations of suspected Monopolistic Conduct by the Anti-Monopoly Law Enforcement Authority shall be carried out by at least two enforcement officers and such officers shall present law enforcement certificates.

The enforcement officers shall maintain written records of their inquiries and investigations. Such written records shall be signed by the persons questioned or investigated.

#### **Article 41**

The Anti-Monopoly Law Enforcement Authority and its staff shall keep confidential commercial secrets obtained during the course of law enforcement.

#### **Article 42**

The undertakings being investigated, interested parties, or other relevant organizations or individuals shall cooperate with the Anti-Monopoly Law Enforcement Authority with respect to the performance of its functions in accordance with the Law and shall not refuse or hinder the investigation by the Anti-Monopoly Law Enforcement Authority.

#### **Article 43**

The undertakings being investigated and interested parties shall have the right to state their opinions. The Anti-Monopoly Law Enforcement Authority shall verify the facts, justifications and evidence presented by the undertakings being investigated and interested parties.

#### **Article 44**

After investigating and verifying the suspected Monopolistic Conduct, if the Anti-Monopoly Law Enforcement Authority determines that such conduct constitutes Monopolistic Conduct, it shall make a decision in accordance with the law and may publicize the decision to the public.

#### **Article 45**

With respect to a suspected Monopolistic Conduct being investigated by the Anti-Monopoly Law Enforcement Authority, if the undertakings being investigated commit

themselves to take specific measures within the time limit approved by the Anti-Monopoly Law Enforcement Authority to eliminate the effects of such Monopolistic Conduct, the Anti-Monopoly Law Enforcement Authority may decide to suspend the investigation. The decision to suspend the investigation shall expressly state the specific commitment made by the undertakings being investigated.

If the Anti-Monopoly Law Enforcement Authority decides to suspend the investigation, it shall monitor the undertakings' performance of their commitments. If the undertakings have fulfilled their commitments, the Anti-Monopoly Law Enforcement Authority may decide to terminate the investigation.

The Anti-Monopoly Law Enforcement Authority shall resume the investigation if one of the following circumstances occurs:

- (1) the undertakings fails to fulfil their commitments;
- (2) material changes have occurred with respect to the facts based on which the decision to suspend the investigation was made;
- (3) the decision to suspend the investigation was made based on incomplete or untrue information provided by the undertakings.

## **Chapter Seven Legal Liabilities**

### **Article 46**

If the undertakings conclude and implement Monopoly Agreements in violation of relevant provisions of this Law, the Anti-Monopoly Law Enforcement Authority shall order the undertakings to stop such illegal act, confiscate their illegal gains and impose fines of more than 1% and less than 10% of their sales in the preceding year; if the Monopoly Agreement has not been implemented, fines of less than RMB 500,000 may be imposed.

If the undertakings, on their own initiative, report to the Anti-Monopoly Law Enforcement Authority information concerning the conclusion of Monopoly Agreements and provide important evidence, the Anti-Monopoly Law Enforcement Authority may reduce the penalty imposed or grant exemption from penalty after weighing the relevant circumstances.

If trade associations organize undertakings within their respective industries to conclude Monopoly Agreements in violation of this Law, the Anti-Monopoly Law Enforcement Authority may impose a fine of no more than RMB 500,000; if the circumstances are serious, the authority in charge of registration and administration of social organizations may revoke the registration of the trade organizations in accordance with the law.

### **Article 47**

If the undertakings abuse their Dominant Market Positions in violation of relevant provisions of this Law, the Anti-Monopoly Law Enforcement Authority shall order the undertakings to stop such illegal act, confiscate their illegal gains and impose a fine of more than 1% and no less than 10% of their sales in the preceding year.

#### **Article 48**

If the undertakings implement the concentration in violation of relevant provisions of this Law, the Anti-Monopoly Law Enforcement Authority under the State Council shall order the undertakings to stop implementing the concentration, dispose of equity or asset within a specified time limit, transfer their business within a specified time limit or take other necessary measures to revert to the condition of the undertakings before the concentration and may impose a fine of no more than RMB 500,000.

#### **Article 49**

The Anti-Monopoly Law Enforcement Authority shall take into consideration the nature, extent and duration of the illegal act and other factors in determining the specific amount of the fines set forth in the Articles 46, 47 and 48 of this Law.

#### **Article 50**

Undertakings that cause loss to others as a result of their Monopolistic Conduct shall be liable for civil liabilities in accordance with the laws.

#### **Article 51**

If administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs abuse their administrative power and engage in activities eliminating or restricting competition, their superior authority shall order them to make correction; the chief officer directly responsible and other persons who are directly responsible shall be subject to disciplinary sanctions in accordance with the law. The Anti-Monopoly Law Enforcement Authority may propose to the relevant superior authority as to how to address the issue in accordance with the laws.

If there are other provisions in laws and administrative regulations concerning the regulation of actions eliminating or restricting competition that are taken by administrative agencies and organizations empowered by laws and regulations to have the function of administering public affairs that abuse their administrative powers, such other provisions shall prevail.

## **Article 52**

If any individual or organization refuses to provide relevant materials or information, or provide false materials or information, or conceal, destroy or remove evidence, or take other action to refuse or hinder the investigation conducted by the Anti-Monopoly Law Enforcement Authority in accordance with the law, the Anti-Monopoly Law Enforcement Authority shall order such individual or organization to make correction. The Anti-Monopoly Law Enforcement Authority may impose a fine of less than RMB 20,000 on individuals or a fine of no more than RMB 200,000 on organizations; if the circumstances are serious, a fine of more than RMB 20,000 and less than RMB 100,000 may be imposed on individuals and a fine of more than RMB 200,000 and less than RMB 1,000,000 on organizations; if any conduct constitutes a criminal offence, the relevant individual or organization shall be prosecuted for criminal liability in accordance with the law.

## **Article 53**

If any individual or organization objects to the decision made by the Anti-Monopoly Law Enforcement Authority in accordance with Articles 28 and 29 hereof, they may first apply for administrative review in accordance with the law; if they object to the decision of the administrative review, they may file an administrative lawsuit in accordance with the law.

If any individual or organization objects to decisions made by the Anti-Monopoly Law Enforcement Authority other than those specified in the preceding paragraph, they may apply for administrative review or file an administrative lawsuit in accordance with the law.

## **Article 54**

Any staff of the Anti-Monopoly Law Enforcement Authority who abuse their powers, fail to fulfil their duties, conduct irregularities for personal gains, or disclose commercial secrets obtained in the course of law enforcement shall be prosecuted for criminal liabilities in accordance with the law if their conducts constitute criminal offences, or shall be subject to disciplinary sanctions in accordance with the law if their conducts do not constitute criminal offences.

## **Chapter Eight Supplementary Provisions**

## **Article 55**

*This law shall not apply to Undertakings' conducts that are exercising their intellectual property rights in accordance with the provisions of laws and administrative regulations relating to intellectual property rights. However, this law shall apply to Undertakings'*

conducts that eliminate or restrict competition by abusing their intellectual property rights.

**Article 56**

This law shall not apply to the alliance among or concerted actions by farmers and the farmers' economic organizations in connection with the production, processing, sales, transportation, and storage of agricultural products and other business activities related to agricultural products.

**Article 57**

This law shall become effective as of August 1, 2008.

# **Guide on Antimonopoly Law Enforcement in the Field of Intellectual Property Rights ('AML IP Guideline')**

(Fifth draft by the State Administration for Industry and Commerce Task Force)

## **Chapter I General Provisions**

### **Article 1 Purpose and basis**

In order to clarify the principles and methods used by the State Council Antimonopoly Law enforcement agencies in the field of intellectual property antimonopoly enforcement, and to improve the transparency of law enforcement, and to provide guidance for undertakings in exercising intellectual property rights, this Guide is enacted in accordance with the relevant provisions of the Antimonopoly Law of the People's Republic of China (hereinafter referred to as "Antimonopoly Law").

### **Article 2 Relationship between intellectual property law and antimonopoly law**

Intellectual property law and Antimonopoly Law have different roles and approaches, but they share a common goal and function, namely, to promote innovation and competition, improve efficiency, and to safeguard consumer interests and public interests.

Antimonopoly Law does not apply when undertakings behave in accordance with intellectual property law and administrative regulations in exercising intellectual property rights; however, Antimonopoly Law applies when undertakings abuse intellectual property rights or eliminate and restrict competition.

### **Article 3 Abuse of intellectual property rights and its relationship with monopolistic behavior**

The abuse of intellectual property rights refers to the act of unfairly exercising intellectual property rights in violation of the boundaries and purposes of the relevant intellectual property laws and administrative regulations, which harms others' interests and public interests.

The abuse of intellectual property rights can constitute violations of different natures according to the specific circumstances, and of these behaviors eliminating and restricting competition can be recognized as monopolistic behaviors under the Antimonopoly Law.

### **Article 4 The nature and type of monopolistic behavior in abuse of intellectual property rights**

Abusing intellectual property rights which eliminates and restricts competition is not one single, independent kind of monopolistic behavior. Under the Antimonopoly Law, this can comprise three kinds of monopolistic behavior respectively or simultaneously according to the nature and manifestation of the acts:

(1) Undertakings abuse intellectual property rights to enter into monopolistic agreements;

(2) Undertakings abuse their dominant market positions mainly achieved as a result of their intellectual property rights;

(3) Undertakings concentrations centering on intellectual property rights which have or may have the effect of eliminating or restricting competition.

### **Article 5 Intellectual property Antimonopoly Law enforcement agencies**

The State Council Antimonopoly Law enforcement agencies are responsible for intellectual property antimonopoly law enforcement in accordance with the "Antimonopoly Law" and this Guide.

Based on operational needs, the State Council Antimonopoly Law enforcement agencies may authorize the corresponding institutions of the People's Government at the levels of provinces, autonomous regions and municipalities, for work related to intellectual property antimonopoly law enforcement, in accordance with the "Antimonopoly Law" and this Guide.

When conducting Antimonopoly Law enforcement work, Antimonopoly Law enforcement agencies can seek the opinion of relevant departments of the State Council in charge of intellectual property rights on specialized problems involved in a case.

### **Article 6 Scope of application**

Intellectual property rights in this guide include the property rights set forth in the laws and administrative regulations such as the Patent Law of the People's Republic of China, the Trademark Law of the People's Republic of China, the Copyright Law of the People's Republic of China, the Law of the People's Republic of China for Countering Unfair Competition and the Regulations of the People's Republic of China on the Protection of New Varieties of Plants, the Regulations for the Protection of Layout-design of Integrated Circuits, and the Regulation for Computer Software Protection.

This Guide applies to the act of abusing intellectual property rights which eliminates and restricts competition in the People's Republic of China. This Guide also applies to the act of abusing intellectual property rights outside the People's Republic of China in a way which eliminates and restricts competition in the domestic market.



## **Chapter II Basic Analytical Framework**

### **Article 7 General steps of analysis in the field of intellectual property rights**

In analyzing the monopolistic behavior of undertakings regarding alleged abuse of intellectual property rights, the State Council Antimonopoly Law enforcement agencies generally take the following steps:

- (1) determining the nature and form of the undertakings' acts in exercising intellectual property rights;
- (2) determining the nature of the interrelationship between undertakings exercising intellectual property rights;
- (3) defining the relevant market where intellectual property rights are being exercised;
- (4) identifying the market position of the undertakings exercising intellectual property rights;
- (5) analyzing the impact of the act of exercising intellectual property rights by the undertakings on competition in the relevant market;
- (6) if the undertaking exercises intellectual property rights in a way which eliminates or restricts competition in the relevant market, conducting further analysis as to the positive effects brought about by the behavior and whether the positive effects outweigh the adverse effects caused by eliminating or restricting competition in the relevant market.

### **Article 8 Definition of the relevant intellectual property markets**

State Council Antimonopoly Law enforcement agencies, in conducting intellectual property Antimonopoly Law enforcement, need to define the relevant market in accordance with the "Guidelines on the Definition of Relevant Market" published by the Antimonopoly Commission of the State Council. The relevant product market and the relevant geographic market are each defined with particular consideration of the impact of factors such as intellectual property rights and innovation.

The relevant product markets where intellectual property rights are involved in Antimonopoly Law enforcement can be technology markets and can also be product markets comprising specific intellectual property rights.

As intellectual property rights have the attributes of commodities in themselves, based on factors such as characteristics, usage and price of the intellectual property right, a group or a category of intellectual property rights which consumers believe to be possessing a relatively close substitution relationship can be defined as the relevant technology market.

As intellectual property rights often attach to particular products, based on factors such as characteristics, usage and price of the product, a group or a category of products with the

same type of intellectual property rights which consumers believe to have a relatively close substitution relationship can be defined as the relevant product market.

#### **Article 9 Intellectual Property and Dominant market position**

State Council Antimonopoly Law enforcement agencies treat intellectual property rights in the same manner as other property rights when enforcing Antimonopoly Law, and will not automatically presume the dominant market position of an undertaking in the relevant market because of its possession of intellectual property rights.

When intellectual property rights constitute an important and even crucial factor for an undertaking to gain market dominance, the State Council Antimonopoly Law enforcement agencies will conduct an analysis in accordance with the general principles and methods of the "Antimonopoly Law" on the identification and presumption of a dominant market position.

#### **Article 10 Factors relevant to the analysis of the impact of exercising intellectual property rights on competition**

The State Council Antimonopoly Law enforcement agencies will consider the following factors (but not limited to) when it analyzes the impact of exercising intellectual property rights on competition:

- (1) the market positions of each of the undertakings exercising intellectual property rights, the trading counterparties and the competitors;
- (2) the degree of concentration of the relevant market;
- (3) the degree of difficulty in entering and exiting the relevant market;
- (4) the existence of industry practices and the degree of industrial development;
- (5) conditions restricting the exercise of the intellectual property rights, such as length and scope of their application;
- (6) the impact of exercising intellectual property rights on promoting innovation and technology;
- (7) the innovative capability of the undertaking and the speed of technological change.

#### **Article 11 Assessment on the impact of exercising intellectual property rights on competition**

The adverse impact or possible adverse impact of exercising intellectual property rights on competition may be shown as elimination or restriction of existing competition, such as reducing the number of competitors in the relevant market through acquisition of intellectual property rights or exclusive licenses, or eliminating existing competition among original

undertakings through cross-licensing agreement of intellectual property rights; this impact may manifest as elimination or restriction of potential market competition, such as refusing to license intellectual property, controlling key technology and other resources, or imposing or raising entry barriers of the relevant market, so as to prohibit other undertakings from obtaining those resources on reasonable terms and prevent the entry of potential competitors.

The actual or potential pro-competitive effects of exercising intellectual property rights may manifest as an improvement in production efficiency or resource utilization through innovation or dissemination and utilization of technology etc, but the aforementioned efficiency must also meet the following criteria:

- (1) The improvement in efficiency is objective and can be proved;
- (2) The restrictive act of the intellectual property right holder is indispensable to the production of efficiency;
- (3) The efficiency generated must be capable to be shared by consumers;
- (4) The restrictive act of the intellectual property right holder will not substantially restrict competition in the relevant market.

Even where the exercise of the intellectual property right exercise will or may potentially result in anticompetitive effect, provided that the undertaking can prove that the exercise of that intellectual property right has or potentially has pro-competitive effects, and that the pro-competitive effects outweigh the anti-competitive effects, the State Council Antimonopoly Law enforcement agencies may permit such an act.

## **Article 12 Impact of the relationship between undertakings and their market positions on competition analysis**

As the impact on competition differs according to the relationship between undertakings and their market positions, in order to improve efficiency and conserve law enforcement resources, the State Council Antimonopoly Law enforcement agencies focus on competing undertakings as well as undertakings that have or jointly have high market shares when analyzing the impact of the exercise of intellectual property rights on competition.

If an undertaking satisfies one of the following circumstances, its exercise of intellectual property rights such as licensing of its IPR can be regarded as having a insignificant impact on competition in the relevant markets, and the State Council Antimonopoly Law enforcement agencies may decide not to initiate an investigation, unless the conduct concerning the exercise of intellectual property rights concern those set out in items (1) to (5) of Article 13 and items (1) to (2) of Article 14 of these Guidelines:

- (1) The total market share of undertakings with competing relationships in the relevant market does not exceed 20 percent; where market shares cannot be calculated, there should be

at least four other undertakings in the relevant market possessing alternative intellectual property rights;

(2) The respective market share of both the undertaking and the trading counterparty in the relevant market is less than 30 percent; where market shares cannot be calculated, there are at least two other undertakings in the relevant market possessing alternative intellectual property rights.

### **Chapter III Antimonopoly Analysis of the Exercise of General Types of Intellectual Property Rights**

#### **Article 13 Agreement between competing undertakings involving intellectual property rights**

Competing undertakings are prohibited from concluding the following monopoly agreements involving intellectual property rights in accordance with Article 13 of the Anti-monopoly Law:

(1) fix or change license fees of intellectual property rights or prices of products with intellectual property rights;

(2) restrict the quantity of intellectual property licenses or the production or sales volume of products with intellectual property rights;

(3) divide the intellectual property right licensing market, or the sales or raw material purchase market where the product contains intellectual property rights;

(4) restrict the purchase or development of new technologies or new equipment or new products with intellectual property rights;

(5) jointly refuse to license intellectual property rights to certain trading counterparties, or jointly refuse to sell products with intellectual property rights to certain trading counterparties;

(6) other monopoly agreements deemed by the State Council Antimonopoly Law enforcement agencies as abusing intellectual property rights.

#### **Article 14 Agreements among undertakings and their trading counterparts involving intellectual property rights**

Undertakings are prohibited from reaching the following agreements involving intellectual property rights with their trading counterparts pursuant to Article 14 of the Antimonopoly Law:

(1) fixing the prices of commodities being resold to a third party that contain intellectual property rights;

(2) restricting the minimum prices for commodities being resold to a third party that contain intellectual property rights; and

(3) other anticompetitive agreements determined to be an abuse of intellectual property rights by the State Council Antimonopoly Law enforcement agencies.

#### **Article 15 Non-prohibited circumstances**

The provisions of Article 13 and 14 of this Guide shall not be used to prohibit agreements among undertakings involving intellectual property rights where it can be proven that the agreements comply with Article 15 of the Antimonopoly Law.

#### **Article 16 Abuse of dominant market position achieved largely through intellectual property rights**

When an undertaking holds a dominant market position that was achieved largely through intellectual property rights, the State Council Antimonopoly Law enforcement agencies will apply Article 17 of the Antimonopoly Law and Chapter II of this Guide to analyze and determine whether the following conduct constitute an abuse of an undertaking' dominant position:

(1) licensing intellectual property rights at unfairly high prices;

(2) without justifiable reasons, refusing to license intellectual property rights;

(3) without justifiable reasons, requiring trading partners to obtain their relevant intellectual property rights exclusively from the undertaking or a designated entity of the undertaking;

(4) without justifiable reasons, tying intellectual property rights or adding other unreasonable trading conditions involving intellectual property rights;

(5) without justifiable reasons, applying differential licensing fees and other licensing terms among comparable trading counterparts; or

(6) other acts determined by the State Council Antimonopoly Law enforcement agencies to be an abuse of an undertaking' dominant market position where that position was achieved largely through intellectual property rights.

#### **Article 17 Refusal to license intellectual property rights**

The "refusal to license intellectual property rights" referred to in Subsection (2) of Article 16 of this Guide refers to a refusal by intellectual property rights holders to license intellectual property rights to other undertakings for reasonable use. The refusal to license is a form of exercising a rights holder' intellectual property rights. Under normal circumstances, the State Council Antimonopoly Law enforcement agencies will not impose an obligation on

intellectual property rights holders to transact with competitors or trading counterparts.

In the course of an undertaking's exercise of its intellectual property rights, the State Council Antimonopoly Law enforcement agencies generally will not deem an undertaking's unilateral refusal to license to other undertakings a violation of the Antimonopoly Law when that refusal is unconditional or non-discriminatory. However, refusals to license intellectual property rights that fall under one of the following categories may be deemed by the State Council Antimonopoly Law enforcement agencies to be a violation of the Antimonopoly Law's provision on the abuse of an undertaking's dominant market position:

(1) Undertakings with dominant market positions unfairly, discriminatorily refuse to license their intellectual property rights;

(2) The intellectual property right refused to be licensed by the undertaking with a dominant market position is an essential element for the licensee to compete in the relevant market, such that the refusal to license that intellectual property right will prohibit the licensee from competing effectively in the relevant market, which will adversely impact competition and innovation in the relevant market, and result in consumer needs not being able to be satisfied.

Refusal to license intellectual property rights can also be a means for undertakings to impose other restrictive conditions or to engage in tying. The State Council Antimonopoly Law enforcement agencies will determine the impact on competition by analyzing all relevant restrictive conditions together or by analyzing the tying provisions.

### **Article 18 Tie-in sales involving IPRs**

For the purpose of Article 16, subsection 4 of this guide, tie-in sale involving IPR refers to the right holder, when exercising its IPR through granting license or other means, requires its trading counterpart to accept license of another IPR or to purchase certain products from the IPR holders or its designated third party against the will of the counterparty. The tied-in products or IPR should be of a nature that can be separately sold or licensed with independent consumer demands. The first IPR is referred to as tying product, and the latter IPR or product is referred to as the tied product.

Tying may have adverse impacts on the competitors in the relevant market, in the sense that it excludes other suppliers' trading opportunity in the tied product market and impairs the choices of consumers. However, tying may also benefit competition in the relevant market mainly by way of reduced costs for sales or management.

When evaluating the effect or potential effect of tying on relevant market and competitors, the Antimonopoly Law enforcement agencies of the State Council will consider, among other things, the purpose of the tying, the nature of and relationship between the tying

and tied products, related trading habits, the scope of effect of tying, as well as the actual operating capability of the one exercising tying. Tying that meet all the following criteria may be prohibited by the State Council Antimonopoly Law enforcement agencies:

- (1) the IPR holder has a dominant market position in the tying product market;
- (2) the tying product and the tied products are distinct commodities in terms of their nature and trading habits;
- (3) the tying has material effect on the tied product market, which extends the dominance of the IPR holder in the tying product market to the tied product market, thus eliminating or restricting competition from other undertakings in the tied product market.
- (4) the tie in sale is not reasonable.

#### **Article 19 Unreasonable trading conditions involving IPRs**

For the purpose of Article 16, subsection 4 of this guide, “unreasonable trading conditions involving IPRs” refers to the situation where the IPR holder, when exercising an IPR through licensing or other means, impose the following conditions against the will of the transaction counterparty:

- (1) to require the counterparty to grant back its improved technology exclusively to the IPR holder;
- (2) to prohibit the counterparty from questioning the validity of the right holder’s intellectual property;
- (3) to limit the counterparty, after the expiry of the term of the license agreement, from manufacturing, using, or selling competing goods or using competing technologies;
- (4) to impose any other unreasonable trading conditions as identified by the State Council Antimonopoly Law enforcement agencies.

#### **Article 20 Concentration of business undertakings involving IPR**

Undertakings may by IPR transfer or exclusive license agreement, obtain the key IPRS of other undertakings, and thereby acquiring control or the capacity to exert a decisive influence over other undertakings. In such case, the undertaking should, if the reporting thresholds for concentration are met, make a filing with the State Council Antimonopoly law enforcement agencies in accordance with the Antimonopoly Law and “provisions of the State Council on the Thresholds for Notification of Concentration of Business Operators” The Antimonopoly Law enforcement agencies, in accordance with the Antimonopoly Law, as well as published guidelines on review of concentration of business operators, to analyze and determine whether the acquisition of IPR results in eliminating or limiting competition in the relevant market. The agencies will focus on the undertaking’s ability to innovate, the

innovative features of other undertakings, as well as the technology development features in the relevant industry.

The Antimonopoly Law enforcement agencies may, during its review of concentration involving IPRs, impose restrictive conditions such as divestment of IPR in order to reduce the effect of eliminating or restricting competition of certain IPR in relevant technical market.

## **Chapter IV. Antimonopoly Analysis of Certain Specific Types of Behaviors Exercising Intellectual Property Rights**

### **Article 21 Patent Pool**

Patent Pool Arrangement ("Patent Pools") refers to agreement between two or more patent holders to cross-license their respective patents or to grant joint license to third parties through an entity or organization. Such organizations may be joint ventures incorporated for this sole purpose, or entrusted pool participant or independent third-party.

Patent pools may have a positive effect on promoting the integration of complementary technologies, reducing transaction costs, eliminating patent barriers, reducing infringement litigation and its certainties etc.. However in certain circumstances, patent pools may eliminate or restrict competition, therefore antimonopoly analysis is required to determine such effect.

When analyzing the impact of patent pools on relevant markets, the State Council Antimonopoly Law Enforcement Agency shall follow the principles established in Chapter II of this guide and shall also consider the following factors:

- (1) The market position of those who participate in the patent pool, and the nature of the patents;
- (2) Whether the patent pool is open and non-discriminatory, if those who participate in patent pool have a dominant market position; and
- (3) Whether the patent pool is unreasonably blocking third-party technology or restricting the establishment of substitutable patent pools.

Patent pools containing only complementary patents generally do not adversely affect competition; the effect of patent pools with substitutable patents will be examined by the State Council antimonopoly agencies case by case.

The following terms of a patent pool license agreement may have the effect of eliminating or restricting competition:

- (1) Prohibiting patentees from independently licensing patents outside of the patent pool;
- (2) Forcing licensees to exclusively grant back any improved or developed non-essential patent technologies to the patent pool or the licensor;



(3) Prohibiting the licensee from questioning the validity of patents in a patent pool;  
(4) Without valid justification, charging licensees in the same relevant market different license fees; or

(5) Without valid justification, restricting licensors or licensees from conducting research and development of competing technology independently jointly with third-party.

Restrictive conditions imposed by the administration organization of a patent pool reasonably necessary for the sake of managing its activities generally will not eliminate or restrict competition in the relevant market. However, conduct unreasonably discriminating against certain participants, restricting participants from using the patents in the pool, or facilitating exchange of competitively sensitive information between the participants may have an effect of eliminating or restricting on competition.

## **Article 22 Exercising patent rights during formulation and implementation of standards**

The formulation and implementation of the standard is usually beneficial for unifying technical specifications, promoting technological innovation and safeguarding consumer interests and public interests. However, if a standard contains patented technology and is widely implemented, it may increase the entry cost of other alternative technologies to comply with the standard, possibly resulting in patent holdup. In the standard formulation and implementation process, if it is considered that the patent holder in the exercising of the patent right results or may result in excluding or restricting competition, the State Council Antimonopoly Law enforcement agencies will use the analytical provisions under Chapter II hereof to analyze and decide.

In formulating international, national, industry or local standards, patents holders unilaterally declaring patent licensing terms and price conditions is a manifestation of the exercise of patent rights and in general will not eliminate or restrict the relevant market competition. However, behavior conforming to the following conditions may be a violation of Antimonopoly Law:

(1) the patent holder or patent applicant knows or should have known that its patents or pending patent applications may be included in the relevant standards;

(2) the patent holder or patent applicant fails to disclose relevant information of its patent or already-publicized patent application information in accordance with the policy prescribed by the standard setting organizations or authorities

(3) After the standard has been announced, the patent holder asserts its patents that has been included in the standard;

(4) the conduct causes or is likely to have an adverse effect on competition and

innovation in the relevant market. For example, refusing to grant permission to use its patent on reasonable terms without justification; or discriminating licensees who are of the same condition by imposing differential licensing prices or conditions without justification.

When the patent holder's patented technology is included into national or industrial mandatory standards, the patent holder should clearly state the upper limit of the license fee in the relevant agreement. The license fee caps should not be significantly higher than the fee level before such technology is included in the standard.

### **Article 23 Technical measures of copyright protection**

Copyright holders taking technical measures is conducive to better protection of copyright in the information network conditions, and generally does not eliminate or restrict competition in the relevant market.

If technical measures are adopted by copyright holders as measures to eliminate or restrict competition in the relevant market, for example, as a means to achieve tying of products or intellectual property rights, the State Council Antimonopoly Law enforcement agencies will base on the provisions of Chapter II of this guide to analyze and make determination.

If the undertaking is able to use alternative methods that have less adverse impacts on restricting competition in the relevant market, but does not use it without justification, the Antimonopoly Law enforcement agencies will generally consider the undertaking's use of technical measures as having the effect of eliminating or restricting competition.

### **Article 24 Acts of copyright collective management organization**

Copyright collective management organization is a social group entity established in accordance of the law for the interest of a group of copyright holders, which collectively manages the copyrights or other related rights of the right holders based on the authorization of the right holders. The establishment of copyright collective management organization and the performance of its activities usually facilitate the exercise of rights by individual copyright holder and the timely and legal use of copyrighted works by entities and individuals.

If the copyright collective management organization's activities meet any one of the following conditions, the State Council Antimonopoly Law enforcement agencies will apply the provisions of Chapter II of this Guide to analyze and make determination:

- (1) charging excessively high agency fees or license fees without justifications;
- (2) discriminatory treatment of copyright owners of the same conditions without justifications;

- (3) forcing acceptance of a package of licenses;
- (4) engaging in other activities that are potentially eliminating or restricting market competition in the relevant market.

## **Chapter V Supplementary Provisions**

### **Article 25 Handling of conducts of abusing intellectual property rights and acts to eliminate or restrict competition**

If an undertaking has been identified as abusing intellectual property rights to eliminate or restrict competition, the State Council Antimonopoly Law enforcement agencies will pursue the violator of legal liabilities in accordance with the provisions of the Antimonopoly Law.

### **Article 26 Time of Implementation**

This guide is effective from [ date ].

**Rules of the Administration for Industry and Commerce on the Prohibition of  
Abuses of Intellectual Property Rights for the Purposes of Eliminating or  
Restricting Competition (‘IP Enforcement Regulation’)**

(Draft for Comments, 11 June 2014)

**Article 1**

These Rules are enacted in accordance with the Anti-Monopoly Law of the People’s Republic of China (hereinafter the “AML”) in order to protect competition and encourage innovation as well as to prohibit the abuse of intellectual property rights by undertakings to eliminate or restrict competition.

**Article 2**

The AML shares the same goal with intellectual property protection, which is to promote innovation and competition, improve efficiency and protect consumer welfare and public interest of the society.

The AML does not apply to conducts of undertakings in exercising their intellectual property rights in accordance with relevant intellectual property laws and administrative regulations; however, the AML applies to conducts of undertakings that abuse their intellectual property rights in eliminating or restricting competition.

**Article 3**

“Undertakings” referred to herein shall mean natural persons, legal persons and other organizations producing or trading products, or providing services. “Products” and “services” here include technologies.

“Conducts eliminating and restricting competition by abusing intellectual property rights to restrict or eliminate competition” referred to herein shall mean monopolistic conducts such as implementing monopolistic agreements, abusing dominant market position, etc. by exercising the intellectual property rights in violation of the AML and provisions under applicable laws and administrative regulations in connection with intellectual property rights.

“Relevant market” referred to herein includes both relevant product market and relevant geographic market and shall be defined in accordance with the AML and the Guidelines on the Definition of Relevant Market issued by the Anti-Monopoly Commission under the State Council by taking into account factors such as intellectual property rights, innovation, etc. In the anti-monopoly law enforcement work involving the license of intellectual property rights, relevant product market may either be the technology market or a product market containing

specific intellectual property rights. “Relevant technology market” shall mean the market where technologies involved in the exercise of the intellectual property rights compete with the existing substitutable technologies of the same type.

#### **Article 4**

Undertakings shall not reach monopolistic agreements during the exercise of intellectual property rights.

Undertakings shall not, in the form of exercising intellectual property rights, reach monopolistic agreements as prohibited by Articles 13 and 14 of the AML except to the extent that such undertakings can prove the agreements reached are in compliance with provisions under Article 15 of the AML.

#### **Article 5**

Under any of the following circumstances, the exercise of intellectual property rights by undertakings may not be identified as monopolistic agreements as prohibited by Article 13(6) and Article 14(3) under the AML, except to the extent that evidence to the contrary prove such agreements have the effects to restrict or eliminate competition:

(1) the combined market share of the competing undertakings in the market affected by their behavior is no more than 20%; or there are at least four other alternative technologies which are available at reasonable costs;

(2) Neither the undertaking nor its counterpart has a market share of more than 30% in the relevant market, or there are at least two other alternative technologies which are available at reasonable costs in the relevant market.

#### **Article 6**

Undertakings with dominant market positions shall not, in the exercise of the intellectual property rights, abuse such dominant market positions to restrict or eliminate competition.

Dominant market positions shall be identified or presumed in accordance with Article 18 and 19 of the AML. Possession of intellectual property rights may constitute a factor to determine the dominant market position, provided that an undertaking may not be directly presumed to hold a dominant market position in relevant market only as a result of its possession of intellectual property rights.

#### **Article 7**

*An undertaking with dominant market position shall not refuse without justifications to license other undertakings to use its intellectual property rights on reasonable terms in the*

circumstance that such intellectual property rights constitute essential facilities for manufacturing and operating activities.

Factors to be considered when determining whether the intellectual property rights constitute essential facilities for manufacturing and operating activities include: whether there are reasonable substitutes to such intellectual property rights in the relevant market; whether such intellectual property rights are essential for other undertakings to participate in competition in the relevant market; whether refusal to license such intellectual property rights will bring adverse impact on the competition or innovation in the relevant market; whether the licensing of such intellectual property rights will result in unreasonable damage to such undertaking, etc..

### **Article 8**

Undertakings with dominant market positions shall not, in the course of exercising their intellectual property rights, engage without justifications in the following behaviors to restrict transactions:

- (1) to restrict that the counterpart can only conduct transactions with them;
- (2) to restrict that the counterpart can only conduct transactions with the undertakings designated by them;
- (3) to restrict that the counterpart shall not conduct transactions with their competitors.

### **Article 9**

Undertakings with dominant market positions shall not, in the course of exercising their intellectual property rights, engage without justifications in tying behaviors satisfying both of the following conditions:

- (1) To require the counterpart to accept against its wills other intellectual property rights or other products or services when licensing or transferring an intellectual property right;
- (2) the tying product and the tied product are two separate products in terms of both nature and trade practice; and
- (3) the tying behavior enables such undertakings to extend their dominant positions in the tying product market to the tied product market, thereby restricting or eliminating the abilities of other undertakings to compete in the tying or tied product market.

### **Article 10**

Undertakings with dominant market positions shall not, in the course of exercising their intellectual property rights, impose without justifications the following unreasonable restrictive conditions:

(1) to require the counterpart to exclusively license back the technology improved by such counterpart;

(2) to prohibit the counterpart from challenging the validity of their intellectual property rights;

(3) to restrain the counterpart from, upon the expiration of the license agreement, manufacturing, using or selling competing products, or developing or using competing technologies in a way that will not infringe their intellectual property rights;

(4) to require the counterpart to continue to pay royalties for intellectual property rights for which the protection period has expired or which have been determined as invalid;

(5) to prohibit the counterpart from engaging in transactions with any third party;

(6) to require the counterpart to impose other unreasonable restrictive conditions.

#### **Article 11**

Undertakings with dominant market positions shall not, in the course of exercising their intellectual property rights, treat counterparts of same conditions in a discriminating manner.

#### **Article 12**

Undertakings shall not, in the course of exercising intellectual property rights, engage in behaviors to eliminate or restrict competition by taking advantage of patent pools.

Members to the patent pool shall not, by taking advantage of such patent pool, exchange competition-related sensitive information concerning price, output, market division, etc. They may also not conclude monopolistic agreements prohibited by Article 13 and Article 14 of the AML, except to the extent that they can prove the agreements concluded are in compliance with provisions of Article 15 of the AML.

Undertakings with dominant market positions or the management organization of the patent pool shall not engage in the following behaviors to abuse dominant market positions by taking advantage of the patent pool:

(1) to restrain member to the pool from licensing patents beyond the pool as independent licensor;

(2) to restrain members to the pool or the licensee from developing independently or jointly with third parties technologies which compete with the pooled patents;

(3) to force the licensee to exclusively license back the technologies it has improved or developed to the management body of, or members to the patent pool;

(4) to prohibit the licensee from challenging the validity of the pooled patents;

(5) to provide differential treatment on trading conditions against members with same conditions to the pool or the licensees in the same relevant market.

For the purpose of these Rules, “patent pool” refers to a scheme of arrangement whereby two or more than two patent holders jointly license their respective patents to a third party in a form where a joint venture is set up specifically for such purpose or a member to the pool or an independent third party is entrusted with the responsibilities of management.

### **Article 13**

Undertakings shall not, in the course of exercising intellectual property rights, engage in behaviors to eliminate or restrict competition by taking advantage of the formulation and implementation of standards (including mandatory requirements of national technological specifications, the same hereinafter).

Undertakings with dominant market positions, without justifications, shall not engage in the following conducts during the process of standard setting and standard implementation:

(1) Where they are aware their patents may be included in relevant standards, refusing to disclose to standards formulation organization the information on their rights or expressly abandoning their rights and asserting their patent rights against the party implementing such standards after such patents become some particular mandatory standards.

(2) After their patent technology become standard essential patents, violating the fair, reasonable and non-discriminatory principle and refusing other undertakings to implement such patents on reasonable terms, or engaging in patent licensing with unfair conditions, or engaging in tying activities during its patent licensing process.

For the purpose of these Rules, the standard essential patents refer to such patents which are indispensable for the implementation of the standard.

### **Article 14**

Collective management organizations for copyrights shall not, in the course of their activities, abuse intellectual property rights to eliminate or restrict competition.

The relevant agreements reached by collective management organizations for copyrights and other undertakings or collective management organizations for copyrights in other countries and regions shall not unreasonably restrict membership qualifications, geographic scope, etc., or restrict the freedom of choice of copyright holders or copyright users.

Collective management organizations for copyrights which have dominant market positions shall not, without justifications, engage in the following behaviors to abuse dominant market positions:

- (1) withholding copyright licenses from others;
- (2) treating copyright holders or licensees of the same conditions differentially;
- (3) forcing the licensee to accept the copyright license it does not need.



(4) restricting copyright holders' right to withdraw from the organization.

For the purpose of these Rules, "collective management organizations for copyrights" refer to social organizations which are established in accordance with laws for the benefit of the copyright holders and the copyright-related right holders ("Right Holders") and manage on a collective basis the copyrights of the Right Holders or the copyright-related rights.

#### **Article 15**

Undertakings with dominant market positions shall not, upon the expiration or invalidation of their intellectual property rights or in the circumstance that sufficient evidence has been provided by other party to prove relevant act does not constitute infringement of intellectual property rights, excessively issue infringement warning letters to eliminate or restrict competition.

#### **Article 16**

Where the undertakings are suspected of abusing intellectual property rights to eliminate or restrict competition, the industrial and commercial authorities shall conduct investigations in accordance with the AML and Provisions on the Procedures for the Investigation and Handling by Industrial and Commercial Authorities of Cases Involving Monopolistic Agreements and Abuse of Dominant Market Positions.

#### **Article 17**

The following measures may be taken for the purpose of analyzing and determining whether the undertakings are suspected of abusing of intellectual property rights to eliminate or restrict competition:

(1) to determine the nature and form of the exercise of intellectual property rights by the undertakings;

(2) to determine the nature of the inter-relationship among the undertakings exercising the intellectual property rights;

(3) to define the relevant market involved in the exercise of intellectual property rights;

(4) to determine the market position of the undertakings exercising the intellectual property rights;

(5) to analyze the impact of the exercise of intellectual property rights by the undertakings on the competition in relevant market;

When analyzing and determine the nature of the relationship among undertakings, it shall be taken into account the characteristics of the act of exercising the intellectual property rights. In circumstance concerning the license of intellectual property rights, the undertakings

previously competing with each other are parties to the license contract, while in the market where both the licensor and licensee manufacture products utilizing such intellectual property rights, the undertakings are competing against each other. However, if the parties were not competing against each other when they executed the agreement, but only became competitors after the execution of the agreement, the agreement will not be deemed as an agreement between competitors unless there is any substantive change to the original agreement.

#### **Article 18**

The following factors shall be taken into consideration when analyzing and determining the impact on competition of the exercise of intellectual property rights by undertakings:

- (1) market positions of the undertaking and its counterparts;
- (2) concentration level of the relevant market;
- (3) difficulty to enter into the relevant market;
- (4) industry practice and development stage of the industry;
- (5) time of restriction in terms of output, geography, consumers, etc. as well as the scope of effectiveness.
- (6) impact on innovation promotion and technology popularization;
- (7) The innovation ability of the undertaking and the speed of technology evolution;
- (8) Other factors relevant to the determination of the impact on competition of the exercise of intellectual property rights.

#### **Article 19**

Where an undertaking abuses its intellectual property rights, eliminating or restricting competition, which constitutes a monopoly agreement, the Administration for Industry and Commerce shall order the undertaking to cease the violation, confiscate the illegal gains, and impose a fine of 1-10 percent of the turnover in the previous fiscal year; where the monopoly agreement has not been implemented, the Administration for Industry and Commerce may impose a fine of no more than RMB 500,000.

Where an undertaking abuses its intellectual property rights, eliminating or restricting competition, which constitutes an abuse of a dominant market position, the Administration for Industry and Commerce shall order the undertaking to cease the violation, confiscate its illegal gains and impose a fine of 1-10 percent of the turnover in the previous fiscal year.

The Administration for Industry and Commerce shall consider the nature, circumstances, seriousness and duration of the violation, and other relevant factors, when determining the specific magnitude of the fine.

**Article 20**

These Rules shall be interpreted by the State Administration of Industry and Commerce.

**Article 21**

These Rules shall take effect as of [ ] 2014.

**Provisions of the Administration for the Industry and Commerce on the  
Prohibition of Abuse of Dominant Market Position**

(Order No.54 of the State Administration for Industry and Commerce)

**Article 4**

*A business operator with a dominant market position is prohibited to refuse to deal with its counterparty in any of the following forms without justifiable reasons:*

1. Reducing the current trading volume with the counterparty;
2. Deferring or terminating a current transaction with the counterparty;
3. Refusing to have new transactions with the counterparty;
4. Imposing restrictive conditions which makes it difficult for the counterparty to continue trading with the business operator; or

*5. Refusing the counterparty's request for using its necessary facilities under reasonable conditions in the course of production and operation.*

*For finding a violation under Item (5), factors such as the following shall be considered comprehensively: feasibility in separately investing in and building or developing such facilities, degree of the counterparty's reliance on such facilities for effective production and operation, possibility of the business operator making such facilities available, and its impact over the production and operation of the business operator.*

## **Provisions against Price Fixing**

(Order No.7 of the National Development and Reform Commission)

### **Article 11**

*A business operator with a dominant market status shall not sell commodities at an unfairly high price* or buy commodities at an unfairly low price.

The following factors shall be considered in the determination of an “unfairly high price” and an “unfairly low price”:

1. whether the selling price or buying price is obviously higher or lower than the price at which other business operators sell or buy the same commodities;
2. whether the selling price is increased or the buying price is lowered beyond the normal range when cost is basically stable;
3. whether the markup rate of the sold commodities is obviously higher than the growth rate of cost or whether the reduction rate of the bought commodities is obviously higher than the decrease rate of cost of transaction counterparty; and
4. other relevant factors that need to be considered.



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