THE US-CHINA BUSINESS COUNCIL
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US-China Business Council Comments on State Council Antimonopoly Commission Draft Antimonopoly Guidelines on Abuse of Intellectual Property Rights (IPR)

November 26, 2015

The US-China Business Council (USCBC) appreciates the opportunity to participate in the public comment process for the State Council Antimonopoly Commission's (AMC) draft Antimonopoly Guidelines on Abuse of Intellectual Property Rights ("draft Guidelines"). This process reflects a continued positive effort by China's key antimonopoly agencies—the National Development and Reform Commission (NDRC), State Administration of Industry and Commerce (SAIC), and Ministry of Commerce (MOFCOM)—to provide greater transparency in the formulation of policy and legislation.

USCBC has approximately 210 member companies, including global leaders in innovation that hold thousands of patents in manufacturing, information technology, pharmaceuticals, services, and other areas. Our companies support China's right to regulate a fair and competitive market, as well as its goals of promoting innovation and competition, enhancing efficiency, and safeguarding consumer and public interests. Developing laws and regulations to promote these goals is the foundation of a modern economy. The comments in this submission represent the views of many leading US companies engaged in business across all industries and sectors in China.

USCBC recognizes Chinese government efforts to provide greater guidance on how antimonopoly agencies should handle intellectual property rights (IPR) issues, as IPR by its very nature differs significantly from other types of property rights. Additionally, we appreciate provisions that recognize that various types of common IPR-related agreements and behaviors—such as grant-backs, joint R&D, patent pools, and high royalty rates—can have both pro-competitive and anti-competitive effects, and can be justified under many circumstances.

At the same time, USCBC member companies have concerns about a number of articles that need clarification to achieve the stated objectives of the draft Guidelines, such as promoting competition and innovation and improving efficiency of the operation of the economy.

Recognizing that there are many provisions of concern that may be addressed in other organizations' comments, USCBC respectfully submits the following comments on the draft Guidelines for clarification and appropriate changes prior to issuing the final version.

Chapter I (General Issues)

(i) Enforcement Principles

We appreciate that these articles seek to lay out guiding principles for antimonopoly enforcement authorities to deal with the unique nature of IPR. The State Council's work to draft these regulations is a testament to that approach, and to the Chinese government's recognition of that uniqueness. However, despite the separate handling of IPR in other Chinese laws and regulations like the Patent Law, the draft Guidelines include principles stating that enforcement officials should "refrain from distinguishing IPR from other property rights."

Given the unique nature of IPR, we recommend that I.i.1 be amended to read "When conducting an antimonopoly analysis on the exercise of IPR, adopt the basic analytical framework provided in the AML, while considering the differences between IPR and other property rights and the legitimate exercise of IPR under the Patent Law and other applicable laws and regulations. Additionally, the legitimate exercise of legally granted IPR shall not be considered to be IPR abuse."

(ii) Definition of Relevant Markets

Section I.ii seeks to clarify key terms such as "technology markets," and introduces the concept of "innovation markets." However, this language raises significant questions for both licensors and licensees because these markets are difficult to define. Given those challenges, the proposed definitions could create challenges for patent licensing. Based on our knowledge, no agency in either of the world's two leading competition jurisdictions—the United States and the European Union—has successfully enforced a case based on either a relevant technology market or a relevant innovation market. In addition, we note that SAIC's April 2015 Regulations on the Prohibition of Conduct that Eliminates or Restricts Competition through IPR Abuse removed language on "innovation markets" during the drafting process in part due to these concerns. Because of the challenges of defining technology markets, these terms should only be used when normal tools of AML analysis—such as defining relevant product markets—are insufficient.

To address these challenges, we recommend removing "When IPR transactions are separated from the trade of relevant products" from the last paragraph of I.ii. This change would appropriately limit the use of "relevant technology markets" to instances in which relevant product markets alone cannot be used to comprehensively assess the competitive impact of the exercise of relevant IPR. This revision is the most targeted way to ensure that the definition of technology markets is invoked in the correct circumstances. We also suggest language be added to clarify how "technologies involved in the exercise of IPR compete with substitutes" will be implemented. This language raises questions about how relevant markets should be defined. Under current language, for example, it is unclear whether new generations of technology will be deemed as substitutes for existing technology despite different features and uses, or whether

agencies might seek to inappropriately define the scope of a relevant market as the scope of a legally granted exclusive patent.

We also recommend the deletion of language in I.ii referring to innovation markets, as the concept is difficult to enforce. Current language does not provide a clear definition, leading to significant questions about how implementation would be possible.

(iii) Overall Analytical Methodology

We appreciate the inclusion in this provision of not only rules for analyzing the competition landscape and how a specific behavior may exclude or restrict competition, but also rules to analyze whether that behavior may facilitate innovation and improve efficiency. This marks an important step toward being able to weigh the pro- and anti-competitive effects of a specific behavior. However, we suggest additional revisions to ensure that this balance is considered in all appropriate cases.

For example, a company licensing a valuable patent could easily trigger all of the factors listed in I.iii.2 (analysis of competition exclusion or restriction), but these factors must be weighed against the pro-innovation and pro-competitive results of extending the borders of useful technology in the China market. To ensure a consistent approach across enforcement agencies, we recommend revising the second sentence of the introductory paragraph to read: "Consideration **shall** be given to the competition landscape in the relevant market, whether the exercise of relevant IPR may exclude or restrict competition, and whether the exercise of relevant IPR facilitates innovation and improves efficiency."

In addition, we suggest further changes to I.iii.3 (analysis of whether the IPR in question facilitates innovation and improves efficiency) to ensure that these provisions are clear and actionable for government authorities. Such changes include:

- I.iii.3.2: Removing the existing requirement that restrictions are "indispensable for facilitating innovation and improving efficiency," and replacing it with language stating that "The restrictive conduct allows exercise of IPR that is useful in making the new technology known to the public and thus advances innovative technology, improves efficiency, or both."

- I.iii.3.5: Providing a clearer definition for "dynamic efficiency," and clarifying any relationship between this term and the term "efficiency" used in I.iii.3.1 and I.iii.3.2.

Chapter II (IPR Agreements Potentially Producing the Effect of Excluding or Restricting Competition)

(i) Grant-backs

We recognize positive language stating that "grant-backs can usually lower licensing risks on the part of the licensor, advance investment and application of new outcomes, and promote

innovation and competition." This provision sits alongside language describing how enforcement officials may determine that some grant-back arrangements are anti-competitive. To ensure consistency with other provisions in the draft Guidelines dealing with compensation, which generally use the term "reasonable," we recommend revising language in II.i.1 from "substantial consideration" to "reasonable consideration."

(ii) Vertical Restrictions

Many of the types of activities listed in II.ii as "vertical restrictions" appear under the Antimonopoly Law as horizontal agreements among competing enterprises (Article 13) as opposed to vertical agreements between business operators and their trading parties (Article 14). This raises questions about the relationship between licensors and licensees. For example, it is unclear whether a patent licensor and licensee have a vertical relationship simply because one is selling a license and the other is buying a license, or if there is another reason. We recommend that the definition of this relationship between licensors and licensees be clarified, and that the title of this section be revised to match. Furthermore, we recommend that the restrictions listed in II.ii then be revised to be consistent with Article 13 and Article 14 of the AML. If the AMC chooses to add new types of monopoly agreements through these regulations, we recommend that the AMC clarify why these specific types of monopoly agreements would be applied to IPR licensing transactions and not to other types of vertical or horizontal relationships.

We also have concerns that some of the types of vertical restrictions listed here may conflict with common market practices. Market-negotiated licensing contracts between enterprises can involve reasonable restrictions on the scope of a licensee's products or where those products are made and sold. These elements should be judged based on their pro- and anti-competitive effects, rather than be deemed in blanket fashion to exclude or restrict competition. We recommend adding language to II.ii recognizing that such restrictions can have both positive and negative competitive impacts.

Additionally, this language may reflect a different approach than that taken in other Chinese laws and regulations. For example, this provision appears to presume that restrictions on use of IPR to specific fields or relevant markets may exclude or restrict competition. However, Article 343 of the Contract Law (and provisions in the 2004 Judicial Interpretation about Application of Laws when Hearing Technical Contract Disputes) allows parties in technology transfer contracts to set the scope within which the licensee can use a patent or technical secret, unless that arrangement restricts technology competition—indicating that these parties are presumed to be permissible unless they are shown to harm competition.

(iv) Patent Pools

We appreciate language in these provisions clearly describing the pro-competitive and anti-competitive elements of patent pools, rather than ruling that patent pools themselves are pro- or anti-competitive. II.iv.4 states that cases where "members of the patent pool share competition-related information such as prices, output, and market segmentation through the patent pool" may be deemed to exclude or restrict competition. This language, however, does not clarify

whether "price" means the price of licensed patents or the price of products that incorporate licensed patents. Given the collective nature of patent pools in ensuring effective licensing of groups of patents, members may need to discuss the total royalty rate for all patents in the pool. To ensure that this language is not broadly applied in ways inappropriate to patent pools, we recommend revising "prices" to "product prices."

Additionally, II.iv.5 states that cases where "members of patent pools and licensees are restricted from developing new technology on their own or by working with a third party" may exclude or restrict competition. This restriction, as written, may inherently prohibit patent pool members from taking action to protect against infringement of their patents by other pool members outside of the patent pool itself. To address this issue, USCBC recommends altering the provision to read: "Members of patent pools and licensees are restricted from developing new technology on their own or by working with a third party, unless such technology development activities infringe upon IPR owned by those members or licensees in ways that violate patent pool rules."

Finally, we note that these provisions do not clarify which parties are liable in the event of an AML investigation—the entity managing a patent pool or the entities providing patents to the patent pool. We suggest the AMC provide clarification on this point, either in the final regulations or in an explanatory notice.

Chapter III (Abuse of Market Dominance Involving IPR)

(i) Unfairly High Royalties

We note the positive addition to this provision permitting "reasonable" economic compensation for IPR licensing, recognition of the importance of recouping R&D investment, and language stating that charging of royalties by a patentee is not subject to the AML. Innovative companies use royalties as a means not only of recouping previous R&D investment, but also of ensuring revenue to fund future innovation, including expanding R&D. We thus recommend that the first sentence be revised to read: "A patentee is entitled to reasonable economic compensation for licensing of its IPR, including funds to recoup R&D investment and to further promote innovation." Additionally, to ensure that enforcement officials adequately consider factors laid out in the first paragraph when weighing the fairness of royalty rates, we suggest the addition of anew factor: "whether collected royalties are appropriate considering the amount of R&D investment or will be used to promote further innovation."

Separately, we encourage the AMC to carefully consider the impact of intervention in royalty rate negotiations between licensing parties to ensure that such interventions do not dampen innovation in China or discourage research into important technological breakthroughs that would require substantial R&D investment.

(ii) Refusal to License

We appreciate the addition of clear language stating that a patent holder is "under no obligation to do transactions with competitors or counterparties." Investigations of refusals to license should be handled carefully, as inappropriate investigations could discourage investment in vital inventions by licensors or encourage them to keep technologies as trade secrets (and not as patents). Inappropriate investigations could also encourage potential licensees to use antimonopoly challenges as a shortcut to gain access to technology as opposed to investing in innovation themselves.

We encourage revisions that bring this provision in line with this fundamental principle. This includes revising the first sentence of the second paragraph from "the justifications for refusing to license" (language that appears to presume that refusing to license is anticompetitive without specific justification) to "whether refusing to license constitutes a conduct of excluding or restricting competition" (language consistent with the first paragraph in assuming that refusal to license is permissible unless determined to be anticompetitive).

The first paragraph of III.ii lists two conditions by which a refusal to license could be considered to constitute the exclusion or restriction of competition. However, both conditions leave questions as to how they would be applied. For example, it would be easy for a patent holder's competitor to allege that a refusal to license could limit competition by claiming that the patented technology is needed for its business, particularly without clearer standards for how to determine "negative influence." Similarly, questions remain about how to determine that no "harm" was caused by a patent holder agreeing to license IPR. We suggest further clarification be provided on how government agencies—and companies—should understand both criteria.

(iv) Impose Unreasonable Terms

We appreciate that this clause defines the scope of "unreasonable terms" in a transaction subject to review, as a way of providing better clarity to all parties in the market where existing antimonopoly enforcement authorities may focus. To further ensure consistent enforcement across antimonopoly enforcement agencies (AMEAs), we recommend additional changes to this language to clarify how AMEAs would handle common business practices such as packaged licensing of patents and how they would assess patentee actions to terminate or freeze its license with a licensee in response to an infringement suit.

We also note that restrictions laid out in III.iv.3 (restrictions on a counterparty from using competing products or technologies) and III.iv.5 (prohibiting a counterparty from trading with third parties or restricting a counterparty from setting trading terms including choice of a counterpart or geographic scope with a third party) both reflect common practices in global licensing, with positive pro-competition and pro-innovation benefits. We encourage the AMC to have further dialogue with global and domestic industry on how best to ensure that these provisions do not unduly restrict common business practices, and revise these measures in line with those discussions.

(v) Discriminatory Treatment

We appreciate language stating that an IPR holder has the right to grant different license terms to different licensees, which can often serve pro-competitive goals by allowing companies to more efficiently serve a variety of consumer groups and by promoting technology development and economic growth.

However, we note that the criteria for determining whether differential treatment of licensees is discriminatory are based largely on whether the terms are the same as other licenses and the cost for the licensor, with little consideration given to the conditions of the licensees. For example, it is a common business practice for a patentee to consider its relationship with the licensee (customer, partner, or competitor), the business conditions of a licensee (wholesaler, retailer, or supplier), where the licensee operates (nationwide or in a few higher-cost markets), and the portfolio assets of a licensee (whether they have patents to license back). Requiring a one-size-fits-all approach will limit China's ability to develop a vibrant, globally respected IP licensing market, and could also undermine the vitality and value of its patents.

Operationally, it is very challenging for government agencies and companies to determine equality of treatment, as technology licenses are increasingly complex and have many substantial and subtly differing terms across parties. In addition, comparing licensees is very challenging, since no two licensees will be the same size, have the same mix of businesses or have the same products.

We recommend that the AMC delete this provision or, if that is not possible, substantially revise it to include new language requiring officials to recognize the complexity of licensing transactions as opposed to requiring equal treatment for all licensees.

Chapter IV (Exercise of IPR Involving Standard-Essential Patents)

We encourage the AMC to approach issues related to standard-essential patents (SEPs) in a way that respects and supports IPR while focusing enforcement measures on clearly defined activities that foreclose competition.

SEPs are a priority concern for many of our member companies, as how China handles issues related to SEPs could have important implications for innovation and technology development. We urge the AMC to engage actively and regularly with industry, including foreign companies and industry groups, on how to define and determine "standard-essential patents" in ways that promote innovation and ensure appropriate support for IP during standard-setting activities.

In addition, we encourage the AMC to carefully consider innovation as it drafts and revises provisions that touch on challenging issues such as the appropriate role of the market in negotiating reasonable royalty rates; common practices such as packaged licensing of patents;

and how to view SEP holders' actions to apply for injunctive relief or respond to an infringement suit.

CONCLUSION

USCBC thanks the NDRC for providing this opportunity to comment on the draft Guidelines. We hope that these comments are constructive and useful to all of those agencies involved in these regulations. We would appreciate the opportunity to have further dialogue on these comments and issues, and would be happy to follow-up as appropriate.

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