

# THE FIRST SECTION

## THE STATE OF INNOVATION IN CANADA: INTELLECTUAL PROPERTY AND COMPETITION LAWS ARE NOT TO BLAME

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Both business and government leaders recognize the importance of innovation. More than half of the 252 Canadian business leaders surveyed recently by the Conference Board of Canada cited innovation as key to their survival.<sup>1</sup> The Commissioner of Competition, Sheridan Scott, emphasized in some of her latest remarks that our companies must continue to innovate if Canada is to prosper in a changing world economy.<sup>2</sup> Despite these good intentions, Canada's record on innovation is lagging.

The Conference Board's recent annual report ranks Canada and other industrialized countries for their performance in innovation, among a number of other areas. In the innovation area, Canada has dropped from third place in 2003 to fourth place in 2004, and is now fifth.<sup>3</sup>

Innovation benefits consumers through the development of new products and services. Innovation is regulated by both intellectual property law and competition law – both help Canadian businesses create new technologies and processes. However, these laws are not to blame for our declining progress in innovation. Canada's laws are similar to those of other countries, such as Finland, Sweden, the United States and Iceland, that are performing better in innovation. A look at the existing legal regime and how these laws are applied demonstrates why they are not the problem.

While intellectual property law and competition law appear on their face to be incompatible – intellectual property law creates limited government-sanctioned monopolies,<sup>4</sup> whereas competition law seeks to eliminate monopoly power in general – they are in fact complementary. They have similar goals but different means of achieving them.

Intellectual property laws grant exclusive and temporary property rights to inventors, thereby providing incentives for innovation, an important type of pro-competitive behaviour. The intellectual property rights holder gets time-limited exclusivity and is protected against unauthorized use of its invention as long as the intellectual property right is still in force.

Intellectual property law allows businesses to innovate and establish markets for their products in the absence of rigorous competition, thereby allowing inventors of new products to recoup the costs of their research and

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development. Without these financial rewards, businesses would have little incentive to innovate and invest in cost-intensive research and development. The hope is that such innovations will be good for consumers in the long run.

Competition law ensures that intellectual property, like other products and services, is not used in an anti-competitive manner as judged by its effect on both markets and the welfare of consumers. Business activities relating to intellectual property may be challenged under the *Competition Act*. The Competition Bureau's approach to applying the Act is set out in its *Intellectual Property Enforcement Guidelines*.<sup>5</sup> The IPEGs state that intellectual property is like any other type of property and the *Competition Act* applies to conduct involving intellectual property rights to the same extent that it applies to conduct involving the exercise of other property rights – with the significant exception of section 32.

The statutory exception in section 32 of the *Competition Act* is a controversial provision that allows a court to impose remedies for even the “mere” exercise of an intellectual property right. The IPEGs state that section 32 of the *Competition Act* permits a court to impose remedies when a rights holder has used its exclusive intellectual property rights to unduly restrain trade or lessen competition. Section 32 allows the Bureau to interfere in the creation of intellectual property rights previously created by the intellectual property regime. While the IPEGs downplay the possible impact of this provision, stating that the Bureau will apply section 32 only in the most unusual circumstances,<sup>6</sup> it would be preferable if section 32 were repealed outright.

A recent Supreme Court of Canada decision and the Competition Bureau's restraint to date in applying the *Competition Act* illustrate how intellectual property law and competition law can be applied effectively to encourage innovation.

In the Supreme Court decision, the Court dismissed a trademark infringement lawsuit by Lego Systems against its rival Mega Bloks.<sup>7</sup> The Court held that Mega Bloks could sell plastic toy blocks that look virtually identical to those made by Lego for over 50 years. Lego's patent under intellectual property laws expired in 1988, and it had tried ever since to extend its exclusive rights using trademark law, another branch of intellectual property law.

The Court found that once an innovator, such as Lego, has received its time-limited reward under the intellectual property regime and that reward has expired, competition should rule. The Court was unimpressed with Lego's attempt to use intellectual property laws and unfair competition to protect its market position. In the Court's view, intellectual property laws “should not inappropriately perpetuate monopoly rights under now expired patents. The market for these products is now open, free and competitive.”<sup>8</sup>

The *Mega Bloks* decision is an important affirmation by Canada's highest court of the need for balance in the granting of intellectual property rights with respect to their length and scope in order to ensure competition and fairness in the market place – ultimately leading to the development and sale of new products. The intellectual property laws were designed to grant exclusive rights to inventors for a limited time, rewarding their innovation appropriately and preserving competition upon expiry of the right. The *Mega Bloks* decision is encouraging for both competition and innovation in Canada.

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Courts and tribunals have only issued a handful of decisions relating to intellectual property under the provisions of the *Competition Act*. All apply the *Competition Act* to intellectual property in a similar manner as to other property. No significant reported decisions have discussed section 32 of the *Competition Act* and its implications for intellectual property law matters since the IPEGs were issued. The IPEGs have elicited very little comment from either the courts or the Competition Tribunal.

To date, the Bureau has rightly not been concerned with the trade-offs already made in the granting of rights under the intellectual property rights regime and has avoided an unnecessary chilling effect on innovation. By interfering with the length and scope in the allocation of intellectual property rights, the Bureau could skew the relative returns that inventors could expect to obtain and could put a chill on innovative conduct.

The Bureau has exercised appropriate restraint in enforcing section 32 of the *Competition Act*. This restraint indicates that the Bureau understands that protecting intellectual property is an important factor in increasing productivity and competition in the Canadian economy.

The Bureau's focus on specific anti-competitive outcomes, as judged by their effect on markets and consumers, is not only an acceptable way to regulate, but preferable to the unnecessary interference in the allocation of intellectual property rights. The Bureau's current approach is objective, transparent and predictable, as is the application of the *Competition Act* to other forms of property. Competition law should apply to all businesses equally. The application of section 32 without the current restraint would amount to a significant restructuring of the Canadian regulatory landscape with the unintended consequences that pro-competitive activities, such as the innovation of new products and services, could be chilled if inventors feared that the Bureau would interfere with their intellectual property rights. Again, it would be better if section 32 were eliminated.

The *Competition Act* gives businesses the flexibility to structure, manage and market their products provided they deliver the right competitive results, with meaningful penalties for any failure to achieve the stipulated competitive outcome. Although there are no rewards for businesses that comply with the rules, the Competition Bureau's current approach specifies what is to be achieved and leaves it to the creativity of businesses to determine how best to innovate while meeting competition law objectives.

As markets change and innovators face global competition and legal uncertainty about ownership of their knowledge-based products, courts and regulators need to continue to carefully apply both intellectual property law and competition law – laws that protect and affect innovation.

Intellectual property law (by defining and protecting intellectual property rights appropriately) and competition law (by managing the use of those rights with restraint) are getting it right. The Conference Board could take note: the application of both these laws, as currently demonstrated, shows that the legal regime is not the reason for Canada's inadequate innovative conduct.

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## Notes

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<sup>1</sup> Canada, The Conference Board of Canada, *Performance and Potential 2005-2006: Trends Reshaping Our Future* (Ottawa: The Conference Board of Canada, 2005).

<sup>2</sup> Sheridan Scott, "Competition Law and Intellectual Property Law: Getting the Balance 'Just Right'" (speech presented to the University of Victoria Faculty of Law International Intellectual Property Law Symposium, July 2006) and "Competition Bureau Progress and Priorities" (speech presented to the Canadian Bar Association Annual Conference on Competition Law, November 2005) [unpublished].

<sup>3</sup> *Supra* note 1 at 36.

<sup>4</sup> Patent law does not necessarily confer on the owner of a patent the right to seek monopoly rents in economic terms. Close substitutes may eliminate the possibility for the inventor to realize these, as with other forms of property. Makan Delrahim, "Contemporary Issues at the Intersection of Intellectual Property and Antitrust" (paper presented to The Fair Competition & Market Economy 2004 Shanghai International Forum) [unpublished].

<sup>5</sup> Canada, Competition Bureau, *Intellectual Property Enforcement Guidelines* (Ottawa: Industry Canada, 2000) [IPEGs].

<sup>6</sup> *Ibid.* at s. 4.2.2.

<sup>7</sup> *Kirkbi AG v. Ritvik Holdings Inc.*, 2005 SCC 65 [*Mega Bloks*].

<sup>8</sup> *Ibid.* at para. 3.

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