

## The Law and Economics of IP enforcement

### The European directive on enforcement of IP rights (adopted April 25 2004)

- In 2003, the **Commission launched** a large scale legislative **initiative to harmonize IP enforcement** across member States, but also to **increase the existing level of enforcement** → the proposal has a clear policy objective:  $\Delta$  level of enforcement  $\rightarrow$   $\Delta$  innovation and creation  $\rightarrow$   $\Delta$  European competitiveness
- After a relatively short legislative period, it has been adopted in April 2004
- The Directive **covers IP in its broadest sense**: Copyright, patent, trademark, but also design, semiconductor topographies, plant variety rights, etc
- The Directive contains rules about the **procedure** to enforce IP rights but also **substantive rules on remedies** for infringement of IP rights, including the possibility (but not the requirement) of **non-civil**, i. e. **criminal Law sanctions**
- Basic **procedural rules**

- i. **Right holders**, their **representatives** and assignees and **collective societies** should have **standing to sue**, and to ask for all civil Law remedies
- ii. Procedures should **not** be unnecessarily **costly, complicated or slow** in order to enforce IP rights
- iii. **Discovery rules favouring right holders**, when there is prima facie evidence of legitimate claim, subject to the protection of confidential information
  - a. Request the defendant to provide evidence
  - b. Request the Court to obtain financial, commercial and bank information
- iv. Measures to ensure and **seize physical evidence** of infringing behaviour, even before proceedings start
  - a. When there may be **irreparable prejudice** to right holder, or risk **of evidence destruction**, injunctions may be decided ***inaudita altera parte***
  - b. May be subject to adequate **guarantees** on the part of right holder
  - c. Requires **suit** within a reasonable period
  - d. Requires **compensation** to defendant when there is no finding of infringement

- v. Right of the IP right holder to **request information** on origin and distribution network of potentially infringing goods
- vi. **Interlocutory injunctions** to prevent impending infringement and continuation of infringement
  - a. When there may be **irreparable prejudice** to right holder, or risk **of evidence destruction**, injunctions may be decided ***inaudita altera parte***
  - b. May be subject to adequate **guarantees** on the part of right holder
  - c. Requires **suit** within a reasonable period
  - d. Requires **compensation** to defendant when there is no finding of infringement
- vii. Measures to ensure **effectiveness of compensation** to the right holder
  - a. **Seizure** of defendant's **assets**
  - b. **Block** of defendant's **assets**
  - c. May be subject to adequate **guarantees** on the part of right holder

## ■ Civil Law remedies

- i. Sanctions should be **effective, proportionate and deterrent** → what is the real meaning of these principles?
- ii. Right holder can claim the **recall** of infringing goods
- iii. Right holder can claim the **disposal** of infringing goods out of the trade channels and with no compensation for infringer
- iv. Right holder can claim the **destruction** of infringing goods with no compensation for infringer
- v. **Injunctive relief** prohibiting continuation of infringement shall be always available in principle
  - a. **Violation** of injunction shall, if provided by National Law, be punished by **effective recurring fines**
  - b. Injunction should **cover** activities of those liable of **contributory or vicarious infringement**
- vi. Injunction and destruction of goods may be **replaced with damages** if
  - Infringement was **innocent** (=non-voluntary, non-reckless and non-negligent)

- Injunction will cause **disproportionate harm to infringer**
  - Right holder would be **reasonably compensated with damages**
- vi. **Damages** for **wilful and negligent** infringement,
- a. **Lump sum on the basis of minimum reasonable royalties** for the use
  - b. **Compensatory damages** (including lost profit, and when appropriate, nonpecuniary harm + recovery of unfair **infringers' profits** due to infringement)
- vii. **Damages** for **innocent** infringement → recovery of profits or damages, which may be pre-established
- vii. **Lawyers' fees** and other expenses
- viii. **Publication** of decision at infringers' expense
- ☐ **Criminal sanctions** → Member States may supplement civil and administrative measures with criminal sanctions
  - ☐ Encouragement of Codes of conduct by professional associations and organisations

## Economic analysis of IP enforcement: Basic principles

- One of the key economic issues in IP enforcement is to **choice between property and liability rules** to protect IP rights and entitlements
- In the categorization of **Kaplow and Shavell** (1996), **IP infringement is closer to taking of things** and not to harmful externalities
- Typically **for takings of things, property rules are recommended**, for the following reasons:
  - i. **Channel transactions into** the framework of **consensual agreements**
  - ii. They **concentrate transactions on the lawful right holder**, saving transaction costs
  - iii. **Avoid** the risk of **retaliatory takings**, or large amount of non-consensual takings
  - iv. **Avoid excessive number of takings** when damages are set too low
  - v. When **taking by multiple parties** is possible, eliminate the **reluctance of right holders to transact**

- vi. Avoid **wasteful expenditures in protecting and taking** rights
  
- ☐ There are some **differential factors concerning IP rights** with ordinary entitlements
  - i. **Non-rivalry in consumption**→ taking does **not deprive the right-holder of the entitlement**, only of its exclusive dimension
  - ii. **No risk of retaliatory or reciprocal takings**
  - iii. **Low value** of some uses **compared to** the level of **transaction costs** necessary to channel them through the market
  - iv. **Large number of potential takers**, not conflicting in use
  
- ☐ There are also some interesting lessons derived from the **economic analysis of Law enforcement**
  - i. **Benefits to the infringers are a social benefit**, which should be taken into account in the social calculus→ proposal directive seems to imply that all infringement is bad. This is particularly dangerous thinking if applied to contributory infringement, which might have (new technologies) large social gains

- ii. Due to the socially costly nature of enforcement, **perfect enforcement is not optimal**, while the proposal seems to have this as a proper goal
- iii. Optimal level of sanction should be such that the expected sanction  **$(p \times S) < \text{Harm}$**
- iv. **Risk aversion** of potential infringers is an important factor → the more risk averse, the lower the level of sanction
  - a. **Many IP infringers are individuals**, and so presumably risk-averse
  - b. Risk aversion of presumptive copyright infringers is higher than of patent and TM infringers (always firms) → **lower magnitude of sanctions in copyright than in patent or TM**
- v. **Damage multiplier** is optimally the inverse of probability of sanction ( $1/p$ ). There should be some **discretion** for the Courts, and **not** a **rigid** legally fixed multiplier
- vi. **Uncertainty** in the determination of level of remedy **favours damages over recovery of benefit** → if there is downward error, infringement will occur under recovery, but not necessarily under damages

- vii. The **directive on enforcement**, maybe surprisingly, does **not include**
  - a. Statutory damages→ at least for Copyright, infringement is commonly of small scale nature→ relatively high fixed cost of pursuing each infringement case leads to underenforcement→ sufficient level of statutory damages will act as an incentive to avoid underenforcement
  - b. No provision for increase in sanction when the infringer is a repeat offender→ economic theory of law enforcement tends to favour higher sanctions for repeat offenders when deterrence is less than optimal, as seems the case of IP rights enforcement