



Improving Canada's Competitiveness: The Key Role of the IP System

Submission to the
Competition Policy Review Panel
by the
Intellectual Property Institute of Canada

January 11, 2008

Introduction

The Intellectual Property Institute of Canada (IPIC) is the professional association of patent agents, trade-mark agents, and lawyers practicing in all areas of intellectual property law. Our membership totals 1,700 individuals, consisting of practitioners in law firms and agencies of all sizes, sole practitioners, in-house corporate intellectual property professionals, government personnel, and academics.

Our members represent small and large businesses throughout Canada, Canadian universities and other institutions with intellectual property rights (e.g. patent, trade-marks, copyright, and industrial designs) in Canada or elsewhere, and foreign companies who do business in Canada, using their intellectual property rights.

Our submission will deal with issues relating to Canada's intellectual property (IP) system. These issues are presented in the context of the Panel's mandate, in particular "with an eye to ensuring that Canada's policies are modern and effective, and reflect a competitive environment that is global in scope and typified by fierce competition between national jurisdictions seeking to attract investment, people and economic opportunities."¹

We have used the consultation paper issued by the Panel as a basis for our submission. In the introduction to the consultation paper, the Panel states: "The Panel is mandated to review key elements of Canada's competition and investment policies to ensure that they are working effectively."²

In the first part of our submission, we will explain why the IP system should be considered as a key factor of Canada's competitiveness.

In the second part, we will make suggestions to improve the effectiveness of the IP system and consequently create "conditions that both encourage Canadian firms to be active and aggressive investors at home and abroad, and maximize Canada's attractiveness as a destination for new investment and talent."³

In this second part, we will address two of the four themes presented in the consultation paper: "Promoting Canadian direct investment abroad" and "Becoming a destination for talent, capital and innovation."⁴

¹ Competition Policy Review Panel, *Sharpening Canada's Competitive Edge, Consultation Paper*, October 30, 2007, p. 1

² Ibid

³ Ibid at p. 2

⁴ The other two themes of the consultation paper being Investment policies and Competition policies.

Part 1: Why Consider the IP System?

A number of reports and studies have established the link between key factors of a nation's competitiveness, as identified in the consultation paper, and the intellectual property system.

a) Foreign direct investment (FDI) and intellectual property

In its 4th Annual Innovation Report, *Including Innovation in Regulatory Frameworks*, the Conference Board of Canada makes the link between the IP system and FDI:

*“Increased competition for FDI stocks. Econometric studies have indicated that, as developing countries raise their intellectual property protection levels, FDI by U.S multinationals tends to shift in favour of those countries and away from more developed economies. So, for example, as Mexico’s intellectual property protection regime continued to converge with the North American intellectual property protection standard, Canada’s share of FDI stock in North America fell markedly from 20.9 per cent to 14.5 per cent between 1990 and 1997. Mexico’s share, on the other hand, rose from 6 per cent to 9.2 per cent during the same period. Several factors may have contributed to Canada’s drop in share; however, survey evidence, as well as empirical work, suggests that the intellectual property regime plays a significant role in determining the inflow of FDI.”*⁵

b) Globalization and intellectual property

The UK government commissioned a comprehensive study of its IP system. The report, prepared by Andrew Gowers, was published in December 2006. Interestingly, many of the points raised in the Gowers Review dovetail the Panel’s consultation paper.

For example, the consultation paper states:

*“Globalization is real, and the implications for Canada’s future are significant. This is not a time for complacency; developments in the global economy compel us to consider how best to move forward.”*⁶

⁵ The Conference Board of Canada, *4th Annual Innovation Report: Including Innovation in Regulatory Frameworks*, 2002, p. 20

⁶ Competition Policy Review Panel, op. cit. p. 15

And the Gowers Review indicates:

“Globalisation and technological advance are changing the shape of the world economy. Increased international trade and investment flows and the emergence of economies such as China and India create great new opportunities for advanced economies such as the UK, but also great challenges. The UK’s comparative advantage in the changing global economy is increasingly likely to come through high value added, knowledge intensive goods and services. The Intellectual Property (IP) system provides an essential framework both to promote and protect the innovation and creativity of industry and artists.”⁷

Consultation paper:

“The objective should not be to insulate Canada from global competition. Rather, the goal is to ensure that the Canadian economic policy framework positions Canada and Canadian enterprises to compete globally. The public policy objective is to maximize opportunity for our domestic firms to grow into global champions and for our existing champions to further expand their reach.”⁸

The Gowers Review:

“Larger markets and fiercer competition present both opportunities and challenges for UK businesses. There are greater rewards for the most innovative firms to compete in ever larger markets. And there are greater pressures on firms to innovate to survive or compete in increasingly competitive global markets. Innovation is therefore key to rising to the challenges and seizing the opportunities of globalisation.

As a consequence, the role of IP in incentivising that innovation has never been more important.”⁹

c) Becoming a Destination for Talent, Capital and Innovation

The Gowers Review:

“Creativity, innovation and investment are crucial to boosting the productivity of the UK economy. Looking forward, their importance is set to remain centre-stage as we enter the ‘third industrial revolution’. The UK must be able to harness creativity and promote innovation in order to

⁷ Her Majesty’s Treasury, *Gowers Review of Intellectual Property*, United Kingdom, 2006, p. 3 (note: Globalization is spelled differently in the Panel’s document and the Gowers Review)

⁸ Competition Policy Review Panel, op. cit. p. 4

⁹ Her Majesty’s Treasury, op. cit. p. 24

compete in the global, knowledge-based economy. Intellectual Property creates the link in the chain which incentivises individuals and firms to innovate and create, with the confidence that their investment is protected.”¹⁰

d) The business environment and intellectual property

Consultation paper:

“However, the global business environment that has evolved over the past 20 years has ushered in a new era, one where governments must formulate policy that reflects a competitive dynamic that has changed fundamentally.”¹¹

The Gowers Review:

“In today’s knowledge economy, IP has never been more important for securing Britain’s prosperity and has never been more challenged by the changing context of innovation: it is estimated that 70 per cent of a typical company’s value lies in its intangible assets, up from around 40 per cent in the early 1980s; and the number of patent applications have more than doubled at the European Patent Office in the last ten years.”¹²

e) The global value chain and intellectual property

Consultation paper:

“The branch plant model has given way to the global value chain mode, with R&D, design and production carried out in various geographic locations. (...)
The challenge for Canada, in regard to both its domestically based MNEs and to attract FDI, is to create an environment that can successfully compete for higher-value activities.”¹³

In a 1999 report for the Council on Competitiveness entitled *The New Challenge to America’s Prosperity: Findings from the Innovation Index*, Professor Michael E. Porter of the Harvard Business School and Professor Scott Stern of MIT Sloan School & NBER, provide the following links between IP and innovation and consequently prosperity.

They identify as the third “policy implication” for the US:

¹⁰ Ibid p. 119

¹¹ Competition Policy Review Panel, op. cit. p. 3

¹² Her Majesty’s Treasury, op cit. p. 34

¹³ Competition Policy Review Panel, op. cit. p. 30

“Third, policies for improving intellectual property protection in areas such as copyrights must become a top priority. As a nation whose assets are increasingly knowledge based, America should be taking the lead in crafting intellectual property tools that address new forms of innovative output and new uses for it.”¹⁴

They chose intellectual property as one of the variables to measure a nation’s innovative capacity. They explain this variable as follows:

“*Strength of Protection for Intellectual Property.* Of the policies affecting national innovative capacity, perhaps the most basic is the provision of appropriate rewards for innovation by private inventors. We measure the extent to which a nation’s policies protect intellectual property rights through patents, copyrights, and the like. Intellectual property protection contributes to national innovative capacity in two ways. First, strict defense of intellectual property encourages domestically based firms to invest in innovative activities and signals the attractiveness of the country as a site in which to locate innovative activity. Second, obtaining the benefits of such protection requires public disclosure of information describing the innovation. In this way, intellectual property protection encourages the diffusion of knowledge throughout the economy.”¹⁵

Finally, and here is the link to global value chains, they present survey results whereby a certain percentage of firms in a specific industry have answered that “IP protection has a major effect on where they invest in R&D facilities”. For the chemical industry, 100% of the firms surveyed agreed that IP protection has a major effect on their R&D investments; it was 80% for the transportation equipment, electrical equipment, metals and machinery industries.¹⁶

This influence of the IP regime on the selection of location for R&D is mentioned also in an article by two World Bank employees:

“One could argue that without strong protection firms may be reluctant to invest in stages of production that involve a significant transfer of proprietary knowledge, such as R&D and technology-intensive manufacturing processes.”¹⁷

Furthermore, the consultation paper comments:

“In this context, the goal for Canada should be to make this country the location of choice for the higher-value elements of these global value chains

¹⁴ Porter, Michael E. and Stern, Scott, *The New Challenge to America’s Prosperity: Findings from the Innovation Index*, Council on Competitiveness, Washington D.C., 1999, p. 8

¹⁵ Ibid p. 27

¹⁶ Ibid, p. 60

¹⁷ Primo Braga, Carlos A. and Fink, Carsten, *The Relationship Between Intellectual Property Rights and Foreign Direct Investment*, Duke Journal of Comparative & International Law, Vol 9: 163, 1988, at p. 173

– whether led by Canadian firms or as part of others’ supply chains – as higher-value productive activity translates into higher wages and salaries, more occupational choice and a better quality of life for Canadians.”¹⁸

The Conference Board of Canada in its Innovation Report stated:

“When a firm is making a decision about where to conduct innovation activities, it will certainly take into consideration the strength of a country’s intellectual protection law. In a globalized world, foreign direct investment in R&D, which is the key conduit of technology transfer and development of new knowledge, flows to jurisdictions where intellectual property rights are securely protected and strongly enforced (...). More importantly, Canadian evidence suggests that a strong intellectual property rights system makes a country an attractive destination for domestic and foreign R&D and patenting activities.”¹⁹

f) Summary

The Conference Board summarized well the key role of IP:

“In summary, if our intellectual property rights environment is not effective enough to protect the return to the inventor, it could considerably weaken Canada’s chance to become a location of choice for increasingly footloose global knowledge assets and R&D investments.

One outstanding question remains: what are some of the ways of creating such an environment?”²⁰

That is what we will address in the next section.

¹⁸ Competition Policy Review Panel, op. cit. p. 6

¹⁹ The Conference Board of Canada, op. cit, p. 15

²⁰ Ibid, p.21

Part 2: Improvements to the IP System

Our comments relate to two themes of the consultation paper: “Promoting Canadian direct investment abroad” and “Becoming a destination for talent, capital and innovation.” IPIC members can bring a unique perspective on these two themes.

First, patent and trade-mark agents are one of the essential links for any Canadian organization wanting to acquire IP rights outside Canada. Many IPIC members work closely with foreign agents to secure IP rights for Canadian innovators around the world. They are keenly aware of the similarities and differences between Canada’s IP system and its counterparts around the world.

Second, foreign organizations wanting to obtain trade-marks and patents in Canada do so with the help of a Canadian trade-mark or patent agent. Agents are therefore one of the first points of contact for foreign companies who are considering doing business in Canada. Our members are well aware of how foreign users of Canada’s IP system view its integrity, efficiency, consistency and dependability.

Current Issues

Overall, Canada has a good, well balanced IP system. Its fundamental protection levels compare well with the systems in other countries.

It could be better, however, when competing with the rest of the world to attract talent, capital and innovation.

Our system has problems that place Canada at a disadvantage and, in recent years, certain events have sent negative signals to the rest of the world about Canada’s IP system.

a) Loss of rights for reasons unrelated to the purpose of the IP system

Canada’s IP legislation is very rigid and can cause a person or organization to lose the right to a patent or trade-mark for reasons that have nothing to do with the fundamental principles of the IP system. This was made obvious, to Canadians and foreign rights owners, in recent events:

- The 2001 *Dutch Industries* decision by the Federal Court put into question the validity of thousands of patents. This was caused because Canada’s “incentive” for small entities to seek patent protection actually puts those patents under unnecessary risks. Unfortunately, the retroactive solution adopted by legislation, while solving the immediate problem, harmed Canada’s reputation further because all the rights holders of the

patents that were at risk, around the world, had to be contacted and were asked to take action.

- The 2003 power outage in Ontario caused at least one company to lose IP rights because it was impossible for Toronto agents to meet a deadline with the Canadian Intellectual Property Office. While the United States had all the mechanisms in place to avoid any loss of rights during the blackout, we did not in Canada. This issue, which affects patents, trademarks, industrial design and copyright has not yet been resolved even though another disruptive event, natural or otherwise, can happen anytime.

b) Protection of confidential communications

Clients disclose confidential information to agents in the course of considering IP protection, drafting applications, and discussing rights between applicants and third parties.

Contrary to the situation in most other major economic jurisdictions, in Canada confidential communications between a client and his/her patent agent or trade-mark agent are not protected from disclosure in litigation.

Such communications are protected by legislation or treaty in:

- Australia
- European Patent Organization (34 member states)
- France
- Germany
- Japan
- Netherlands
- New Zealand
- United Kingdom

This issue affects both the promotion of Canadian investment abroad and foreign investment to Canada.

Regarding Canadian investment abroad, US courts have recognized privilege for communications with an agent from another country, but only if those communications are protected from disclosure in that country. A 1999 case in the US between a French pharmaceutical company and a competitor, in which the French pharma was forced to divulge its communications while the other company was not, prompted France, the Netherlands and the European Patent Organization to adopt statutes to protect communications.

Therefore, companies having employed a Canadian agent can be at a disadvantage when entering IP litigation outside Canada. This affects, for example, Canadian companies and foreign companies who perform R&D in Canada.

Regarding foreign investment in Canada, in December 2006, during litigation between two major pharmaceutical corporations, the judge ordered one company to divulge the confidential communications held with its UK patent agent. This is significant because in the UK, these communications are protected by statute. However they are not in Canada. The judge indicated that the company had to live with the “burdens” of Canada’s system of justice.

The problem with the “burdens” of the Canadian system is that it has the potential of affecting more than just the Canadian operations of a company. Some will hesitate to do business in Canada because it may put their foreign patents at risk.

c) Leadership challenges

Canada is slow to react to changes happening around the world. This does not send a good signal about the importance of IP in Canada. One obvious example is the debate that has been going on for years without resolution about reform of the *Copyright Act*.

Another example is the 2002 decision by the Supreme Court, known as the *Harvard Mouse* decision, that higher life forms are not patentable subject matter in Canada. This issue is of significant economic importance because higher life forms, in terms of patenting, include plants. Canada has an innovative agricultural sector that requires full IP protection. Also, biotechnology activities in Canada involve 2,500 life science organizations, 200,000 jobs and R&D expenditures of \$1.7 billion in 2006²¹. Currently, Canada is out of step with other jurisdictions.

d) Patenting by Canadians lags behind their foreign competitors

There is statistical evidence that there is room for improvement in the IP system and/or the IP culture in Canada.

The Conference Board of Canada, in its June 2007 Report Card on Canada, gave the country a “D” for the measure of triadic patent families²² per million of population.²³ The number is well below the output of most comparator countries.

Furthermore, according to the World Intellectual Property Organization, Canada ranks 18th in terms of resident patent applications per million inhabitants²⁴.

²¹ *The Hill Times, Policy Briefing on Biotechnology*, October 1, 2007, p. 30

²² The measure of triadic patent families is the number of patent applications filed in the three largest patent offices: the European Patent Office (EPO), the Japanese Patent Office (JPO) and the United States Patent and Trademark Office (USPTO).

²³ The Conference Board of Canada, *How Canada Performs: A Report Card on Canada*, June 2007, p. 56

Recommendations

a) Exercise leadership

- The IP system cannot be taken for granted if Canada is to compete in attracting talent, capital and innovation. The government has to exercise leadership in ensuring that the system is competitive. In its 4th Annual Innovation Report, the Conference Board had recommended: “seize the moment to build a forceful vision to articulate the value of intellectual property for Canada.”²⁵
- The following priority actions illustrate how this leadership could be exercised. These actions would send a strong signal inside and outside Canada about the importance given to IP in Canada.

b) Reduce the risks associated with the Canadian IP system

- Modify the various elements of IP legislation and regulation so that rights are not placed at risk for reasons that are not fundamental to the system, for example, when there is an interruption of service.
- Provide statutory protection for the confidential communications between clients and their Canadian patent and trade-mark agents.

c) Recognize the importance of intellectual property assets

- Adopt legislative amendments to combat counterfeiting as proposed by two parliamentary committees.

d) Modernize the regulation of agents

- Create a new regulatory body for patent and trade-mark agents so that agents, who handle property worth millions of dollars, be recognized as true professionals.

e) Become a destination of choice

- With the support of government, the Canadian Intellectual Property Office (CIPO) has to continue working aggressively on improving the

²⁴ World Intellectual Property Organization, *WIPO Patent Report: Statistics on Worldwide Patent Activities*, 2007 Edition, p. 19

²⁵ The Conference Board of Canada, *op. cit.* p. 23

timeliness of patent and trade-mark examination, the quality of service and the IP framework.

These recommendations do not necessitate significant expenses for the government. They can actually feed a virtuous circle because the system is not only self funding (through user fees), it actually brings revenue to Canada. In 2005-06, 87% of the patent applications and 55% of the trade-mark applications originated from outside Canada²⁶. This provides significant revenues in government fees and agent fees to ensure that Canadians benefit from a good IP system. Improvements to the system can have positive impacts on these revenues.

²⁶ Canadian Intellectual Property Office, *Annual Report 2005-2006*

Conclusion

The Panel wants to make recommendations to the government on ways to establish the domestic conditions that both encourage Canadian firms to be active and aggressive investors at home and abroad, and maximize Canada's attractiveness as a destination for new investment and talent.

In making such recommendations, the Panel must consider the IP system.

We have explained why the system is an integral part of the business environment and why it cannot be taken for granted. We have briefly presented recommendations to improve the IP system and consequently enhance Canadian competitiveness.

We would be pleased to provide additional information about these recommendations and look forward to reading the report of the Panel.