

# AntitrustConnect Blog

## Antitrust Law and Intellectual Property: Intersection or Crossroad?

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It is traditional in beginning an article on antitrust law and intellectual property to note the tension?or, as some would put it, the conflict?when the two intersect. And there is certainly support in the earlier case law for that point of view. As the Second Circuit observed in *SCM Corp. v. Xerox Corp.*, 645 F.2d 1195, 1203 (2d Cir. 1981), the antitrust and intellectual property laws “necessarily clash . . . the primary purpose of the antitrust laws to preserve competition can be frustrated, albeit temporarily, by a holder’s exercise of the patent’s inherent exclusionary power during its term.”

In this last two decades, however, a fundamental change in legal perspective has gradually taken place. The courts have provided greater clarity on the exclusionary rights of holders of patents and other intellectual property. *See, e.g., United States v. Microsoft Corp.*, 253 F.3d 34, 63 (D.C. Cir. 2001) (declaring as borderline “frivolous” the software supplier’s position that it has “an absolute and unfettered right to use the intellectual property as it wishes . . .”). And the federal enforcement agencies have made it their stated policy to treat IP as essentially comparable to any other form of property. *See* US Dep’t of Justice & Federal Trade Comm’n, Antitrust Guidelines for the Licensing of Intellectual Property, *reprinted in* 4 Trade. Rep. Rep. (CCH) ¶ 13,132 (1995), also available at <http://www.usdoj.gov/latr/public/guidelines/0558.pdf>. In the process, antitrust law as applied to intellectual property has come to a crossroad in which the once prevailing view that there was conflict, given the disparate treatment of exclusionary conduct, has shifted in the direction of a greater appreciation for the common goals of the two areas of law. This more harmonious view of the antitrust and intellectual property laws was expressed in a 1990 opinion by the Federal Circuit: The “aims and objectives of patent and antitrust laws . . . are actually complementary, as both are aimed at encouraging innovation, industry and competition.” *Atari Games Corp. v. Nintendo of Am., Inc.*, 897 F.2d 1572, 1576 (Fed. Cir. 1990).

This article will begin by providing an overview of the antitrust laws applicable to intellectual property transactions and then go on to identify some specific sources of guidance to IP owners and their counsel. These citations are by no means an exhaustive list of the important legal authorities, but they do offer some general insight into how the courts and enforcement agencies approach the multitude of substantive issues that arise at the intersection of antitrust and intellectual property law.

Next, the article will address three substantive areas in greater detail. First, the antitrust regulation of intellectual property licensing will be discussed, from unilateral refusals to license to multi-party

patent pools. Second, standard setting, in both its *de jure* and *de facto* forms, will be considered a potential source of antitrust restraint. Third, the article will touch briefly upon the topic of settlements of patent infringement litigation, which has generated substantial controversy in the context of the so-called “reverse payment” settlements between brand and generic drug manufacturers.

Finally, the article will list some practical questions that IP owners and their counsel may want to ask when evaluating an intellectual property transaction from an antitrust perspective.

### **Antitrust/IP Law: An Overview**

Holders of patents and other types of intellectual property, besides enjoying the benefits that the law confers on their inventions and works, must navigate a wide array of antitrust rules and regulations. Both §§ 1 and 2 of the Sherman Antitrust Act (15 U.S.C. §§ 1 and 2) are applicable to the licensing and use of intellectual property. Section 1, which covers agreements between two or more parties in restraint of trade, is the primary antitrust law regulating IP licenses. Section 2 of the Sherman Act, concerned with monopolization and attempts at monopolization, regulates unilateral conduct by IP owners who hold a dominant position in a relevant market.

A sale outright of IP or an exclusive license is also subject to antitrust scrutiny under the mergers and acquisitions provisions of the Clayton Act (15 U.S.C. § 18). Moreover, holders of IP face the prospect of antitrust enforcement by both private plaintiffs and the enforcement authorities at the federal and state levels. In addition to the Clayton Act, the Federal Trade Commission (FTC) is also responsible for enforcement of § 5 of the FTC Act, 15 U.S.C. § 45, which gives the agency the statutory authority to enjoin a broader array of anticompetitive conduct.

Since the markets for intellectual property are many times worldwide, its owners must often analyze whether their licensing or use of IP runs afoul of competition law in foreign jurisdictions. In the European Union, technology licensing agreements are analyzed under Article 101 of the Treaty on the Functioning of the European Union (TFEU), formerly Article 81 of the EC Treaty. Despite ongoing efforts by nations at antitrust convergence, important international differences remain in the antitrust regulation of intellectual property transactions.

The language of the principal antitrust statutes is broad and offers little specific guidance to holders of intellectual property. Over the past two decades, valuable antitrust guidance for those holding patents, copyrights, and other IP rights has come in the form of agency guidelines, business review letters, and case law. Here are six of the more significant sources of such guidance.

#### **1. The IP Guidelines**

In 1995, the Department of Justice and the Federal Trade Commission jointly issued Antitrust Guidelines for the Licensing of Intellectual Property (the IP Guidelines). This was a watershed moment in the regulation of intellectual property transactions. Years earlier, a strict set of antitrust rules was applied to the licensing of intellectual property, known as the “nine no-no’s.” *See* Bruce Wilson, Deputy Associated Att’y Gen., Antitrust Div., Department of Justice, Remarks to Michigan State Bar Antitrust Law Section and Patent Trademark and Copyright Law Section (Sept. 21, 1972), in [Current Comment Transfer Binder, 1969-1983] Trade Reg. Rep. (CCH) ¶50,146.

The IP Guidelines set forth a more flexible approach to enforcement, one that more expressly acknowledged the pro-competitive benefits of licensing. Three basic principles were identified: (1)

Intellectual property is essentially comparable to any other form of property; (2) Intellectual property rights are not presumed to create market power; and (3) Intellectual property allows firms to combine complementary factors of production and is generally pro-competitive.

While stating enforcement policy, it is important to bear in mind that the IP Guidelines are not binding on the courts. They have, nevertheless, signaled the general direction US law has taken in the antitrust regulation of intellectual property licensing.

## 2. Business Review Letters

Despite the significance of the IP Guidelines in stating enforcement policy covering the licensing of intellectual property, their broad principles have left many more specific questions unanswered. For example, how exactly does a patent holder decide if a cross-licensing scheme or pooling engagement involving its intellectual property is one that will be considered pro-competitive, by combining complementary factors of production, or conversely will be condemned as an anticompetitive price-fixing conspiracy? Since the issuance of the IP Guidelines, the Federal Trade Commission's generally favorable attitude toward IP licensing has not stopped the agency from initiating enforcement actions against certain licensing arrangements. In 1998, the FTC challenged the pooling arrangement between Summit Technology, Inc. and VISX, Inc. – the only two firms at the time that supplied laser equipment used in vision correcting eye surgery – as a naked price fixing scheme. *Summit Technology*, No. 9286 (FTC Mar. 24, 1998) (complaint). Beyond the IP Guidelines, valuable additional guidance to owners of IP and their counsel can be found in the business review letters issued over the last two decades by the Department of Justice.

In a December 16, 1998, business review letter, the Justice Department identified the specific features of the DVD patent pool that spared it the fate of the Summit/VISX joint venture. (Letter from Joel I. Klein, Assistant Attorney Gen., US Dep't of Justice, to Garrard R. Beeney, Esq. (Dec. 16, 1998) (hereinafter DVD Patent Pool Letter)).

Among the important features of the DVD patent pool were the requirements that only patents “essential” to the technology standards could be contributed and that the licenses were non-exclusive, meaning that each patent holder remained free to license its patents to third parties independent of the pool.

More recently, through business review letters issued to counsel for two standard-setting organizations (SSOs), VITA and IEEE, the Department of Justice provided helpful guidance on the agency's enforcement policy with respect to SSO disclosure requirements. (Letter from Thomas O. Barnett, Assistant Att'y Gen., US Dep't of Justice, to Robert A. Skitol, Esq. (Oct. 30, 2006) (VITA Business Review Letter) and Letter from Thomas O. Barnett, Assistant Att'y Gen., US Dep't of Justice, to Michael A. Lindsey, Esq. (April 30, 2007) (IEEE Business Review Letter)).

SSOs have often required participants in the standard-setting process to disclose their relevant IP in advance and to commit to license on so-called RAND (reasonable and non-discriminatory) terms. To further address the potential problem of patent hold-up, VITA proposed to allow disclosure of maximum royalty rates and IEEE proposed to give the chairman of the working group the authority to ask members for various assurances about future licensing terms. In response, the Department of Justice informed the two SSOs, in separate letters, that it had no present intent to challenge such policies.

## 3. United States v. Microsoft

The US government's 10-year fight against Microsoft and its licensing practices with respect to the Windows operating system was notable both for the enormous public attention brought to the antitrust case and for the 2001 *en banc* decision that ultimately came from the D.C. Circuit Court of Appeals. *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001), *cert denied*, 122 S. Ct. 350 (2001). The *en banc* decision, which affirmed in part and reversed in part the district court's findings on liability and vacated its break-up order, addressed a host of antitrust issues facing patent holders that are found to hold a dominant position in a relevant market. In the course of its opinion, the Court of Appeals seemed to lay to rest the notion that an IP owner had an absolute and unfettered right to use intellectual property as it wishes: "That is no more correct than the proposition that use of one's personal property, such as a baseball bat, cannot give rise to tort liability."

#### 4. Illinois Tool Works

The influence of patent law on the development of antitrust law, particularly as it relates to intellectual property, has deep historical roots. Sixty years ago, patent law was influential to the development of antitrust law applicable to tying arrangements. In particular, the Supreme Court's decision in *International Salt Co. v. United States*, 332 U.S. 392 (1947), that found *per se* unlawful the tying of patented machines to unpatented salt products was influenced by the finding of patent misuse in *Morton Salt Co. v. G.S. Suppieger Co.*, 314 U.S. 488 (1942). In *Illinois Tool Works Inc. v. Independent Ink*, 547 U.S. 28, 39 (2006), the Supreme Court expressly made this connection between the two earlier decisions: "The assumption that tying contracts 'ten[d] . . . to accomplishment of monopoly' can be traced to the Government's brief in *International Salt*, which relied heavily on our earlier patent misuse decision in *Morton Salt*."

In *Illinois Tool Works*, the Supreme Court made clear that no presumption of market power exists. "[I]n all cases involving a tying arrangement, the plaintiff must prove that the defendant has market power in the tying product." Plaintiff has this burden of proof even when the defendant has patent rights with respect to the tying product.

Two factors lead to the ultimate demise of the market power presumption in tying cases involving patented products. First, and more generally, since *International Salt*, "[the] Court's strong disapproval of tying arrangements has substantially diminished." By the 1970s, the Supreme Court was no longer presuming that tying arrangements only served to suppress competition. *See, e.g., United States Steel Corp. v. Fortner Enterprises, Inc.*, 429 U.S. 610 (1977). Second, in 1988, Congress amended the patent code to eliminate the presumption of market power in the patent misuse context. *See* 35 U.S.C. § 271(d)(5) (no relief for patent misuse "unless, in view of the circumstances, the patent owner has market power in the relevant market for the patent or patented product on which the license or sale is conditioned.").

Thus, the foundation for the presumption of market power in antitrust cases, which had been based on *Morton Salt* and other patent law cases, was gone.

#### 5. FTC and DOJ Hearings

In addition to the 1995 IP Guidelines, the two federal enforcement agencies collaborated on a 2007 report, [Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition](#) (the Joint Report). The Joint Report, which followed 24 days of hearings over 10 months, provides further guidance on the agencies' competition views on a variety of IP-related

issues. It discusses refusals to license patents, collaborative standard setting, patent pooling, IP licensing, tying and bundling of IP rights, and attempts to extend patent life beyond the expiration date.

More recently, between December 5, 2008, and May 4, 2009, the Federal Trade Commission held a series of public hearings on “The Evolving IP Marketplace.” A report from the FTC, based on those hearings, is expected soon. Testimony and articles in connection with the FTC hearings are located at [www.ftc.gov/bc/workshops/ipmarketplace](http://www.ftc.gov/bc/workshops/ipmarketplace).

## **6. European Commission’s Block Exemptions**

In the EU, the European Commission applies a two-step analysis to licensing arrangements. First, it considers whether the arrangement restricts competition within the meaning of Article 101(1) of the TFEU. Unlike the rule of reason analysis under the Sherman Act, there is no balancing of pro- and anticompetitive effects under Article 101(1). IP owners considering whether the license implicates Article 101(1) should consider the EC’s Technology Transfer Guidelines. If it does, the Commission then considers whether the licensing arrangement falls within one of the block exemptions pursuant to Article 101(3). The block exemption most directly applicable to licenses of technology is the Technology Transfer Block Exemption.

In November 2000, pursuant to Article 81(3) of the EC Treaty (now Article 101(3) of the TFEU), the European Commission also adopted block exemptions covering specialization agreements (Specialization BER) and research and development agreements (R&D BER), as well as guidelines on the general assessment of horizontal co-operation agreements (Horizontal Guidelines). The current versions of the R&D BER and Specialization BER were set to expire in December 2010. The EC has proposed new block exemptions and revised Horizontal Guidelines. Standard-setting arrangements are a key issue addressed in the proposed new Horizontal Guidelines, which aim to ensure that the benefits of standard-setting are passed on to consumers.

## **Intellectual Property Licensing**

The consensus among the courts and the enforcement agencies, as reflected in the case law and policy guidelines, is that licensing is generally pro-competitive and often essential to realizing the full benefits of patents, copyrights, and other intellectual property. As with other types of agreements, however, IP licenses are subject to review under § 1 of the Sherman Act, among other antitrust provisions, for their potential anticompetitive effects. Below is a discussion of the analytical framework commonly applied in assessing the competitive impact of IP licenses, followed by a summary of some specific licensing issues.

## **Unilateral vs. Concerted Action**

A threshold issue in antitrust analysis is whether the license involves more than one firm or economic unit. In *American Needle, Inc. v. NFL*, 130 S. Ct. 2201 (2010), the football league and its member teams defended the restraints on licensing apparel, in part, on the basis that the defendants constituted a single economic unit and, therefore, no concerted action was involved that implicated § 1 of the Sherman Act. The Supreme Court applied a “functional” analysis in resolving that issue. It considered whether the license joins together separate decision-makers pursuing separate economic interests. For purposes of licensing apparel, the Supreme Court held that there was concerted action by the NFL member teams and, therefore, that the licensing agreement was subject to antitrust scrutiny under § 1 of the Sherman Act.

## Horizontal vs. Vertical Relationship

For purposes of antitrust analysis, IP licenses are often characterized as either horizontal or vertical (IP Guidelines § 3.3). A license is vertical when it affects activities that are in a complementary relationship. For example, if a company involved in research and development licenses its patent rights to a manufacturer that is in a position to use the technology to create finished products, the license will likely be viewed as a vertical one. Vertical licenses will, absent some unusual licensing provision, typically be evaluated under the rule of reason.

In contrast, a license or cross-license of intellectual property between actual or potential competitors in the same relevant market will generally be treated as a horizontal agreement. The relevant market in which such competitive overlap exists may be either the market for the technology being licensed or an innovation market for the development of rival technology. When there is a horizontal relationship between the licensor and licensee, the licensing arrangement will likely be subjected to greater antitrust scrutiny by the courts and the enforcement agencies. That does not mean that horizontal licenses will be presumed to be anticompetitive. It just means that they will be examined to see if any *per se* antitrust offenses are committed by the licensing terms, for example, group boycotts, price fixing, agreements to reduce output, or allocation of markets. Absent such “pernicious” conduct, horizontal licenses will be evaluated, like vertical ones, under the rule of reason.

## Per Se vs. Rule of Reason Treatment

In contrast to the strict standard applicable to *per se* antitrust offenses, the rule of reason analysis used to evaluate most licensing arrangements generally requires a comprehensive inquiry into market conditions to determine whether the pro-competitive effects of the license are outweighed by any anticompetitive effects. Typically, the analysis begins with a definition of relevant products, technology, or innovation market. Definition of a relevant market may not be required if the plaintiff can otherwise demonstrate actual anticompetitive effects. *See, e.g., FTC v. Indiana Fed’n of Dentists*, 476 U.S. 447 (1986). Since the Supreme Court’s decision in *Illinois Tool Works*, it is no longer presumed that the holder of a patent possesses market power. The rule of reason analysis also contemplates a balancing of anticompetitive effects with offsetting pro-competitive effects. An example of pro-competitive effects is a licensing restraint that is shown to facilitate the broader use of the licensed intellectual property.

When there are plausible pro-competitive efficiencies to be gained by the licensing restraint, both the courts and the enforcement agencies will evaluate whether the restraint is “reasonably necessary” to achieving those benefits. The application of that standard is a practical one; the antitrust enforcers will not invalidate the restraint simply because there was an alternative that is theoretically less restrictive but not realistic. *See, e.g., American Motor Inns v. Holiday Inn*, 521 F.2d 1230, 1249-1250 (3d Cir. 1975).

## Specific Licensing Issues

### *Unilateral Refusals to Deal*

While a basic right of IP owners under the Patent Act and the Copyright Act is the right to exclude others from their inventions and works, the courts and the enforcement agencies have never gone so far as to state that a unilateral refusal to license is never a basis for antitrust liability. Section 271(b) of the Patent Act was amended in 1988 to provide that “[n]o patent owner otherwise

entitled to relief for infringement or contributory infringement shall be ... deemed guilty of misuse ... by reason of ... having ... (4) refused to license or use any rights to the patent.” The enforcement agencies and several courts have interpreted § 271(2) as limited to misuse and not necessarily circumscribing the scope of antitrust liability. *See, e.g., Grid Sys. Corp. v. Texas Instruments, Inc.*, 771 F. Supp. 1033, 1037 n.2 (N.D. Cal. 1991). A decade ago, two decisions from the Court of Appeals, *Image Technical Servs. v. Eastman Kodak Co.*, 125 F.3d 1195 (9th Cir. 1997), and *In re Independent Serv. Orgs. Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000), reached opposite conclusions on that licensing issue. In *Kodak*, the Ninth Circuit affirmed liability on the basis of the copier manufacturer’s refusal to sell patented replacement parts. In the *ISO* case, Xerox obtained summary judgment in defense of similar exclusionary conduct. One material difference between the two cases is that Xerox, unlike Kodak, immediately raised intellectual property rights as a defense to the antitrust claims.

Particularly in light of the Supreme Court’s decision in *Verizon Commc’n v. Law Offices of Curtis v. Trinko, LLP*, 540 U.S. 398, 407 (2004), which marginalized the essential facilities doctrine as a source for a unilateral duty to deal, it appears less likely than ever that a unilateral refusal to license will be the sole basis for the imposition of antitrust liability. This does not mean, however, that IP owners can impose restrictive terms in their licenses or *collectively* refuse to license with certain antitrust impunity.

### ***Tying Arrangements***

Tying arrangements exist when the buyer is forced to purchase the “tied” product that the buyer did not want (or would have preferred to purchase elsewhere) in order to obtain the “tying” product from the seller. For bundled licenses, where the owner of the intellectual property has market power in the tying technology and the licensing arrangement has an adverse effect on competition in the tied product, there is the prospect of either a misuse defense in any infringement action involving the technology or the imposition of antitrust liability, or both. *See, e.g., U.S. Philips v. International Trade Commission*, 424 F.3d 1179 (Fed. Cir. 2005).

There are two important limitations on tying claims in the IP context. First, as with other tying claims, a bundling of intellectual property will generally not give rise to antitrust liability on a tying theory if separate licenses are also available on financial terms that are realistic and economically viable. Second, a licensor may successfully defend against a tying claim if it can demonstrate that the tie was technically necessary to enhance the functionality of the product offered to the consumers (*Microsoft*, 253 F.3d at 89 (“there are strong reasons to doubt that the integration of additional software functionality into an [operating system] falls among these arrangements” deserving *per se* antitrust treatment.)).

### ***Resale Price Maintenance***

The law has evolved such that the prospect that a licensor will be subject to antitrust liability for resale price maintenance is significantly diminished. Within a span of 10 years, the US Supreme Court abandoned the *per se* treatment of both maximum resale price maintenance in *State Oil Co. v. Khan*, 522 U.S. 3 (1997) and minimum resale price maintenance in *Leegin Creative Leather Products, Inc. v. PSKS*, 551 U.S. 877 (2007).

Both forms of price maintenance are now subject to the more flexible rule of reason analysis. Still, there is some ongoing risk of *per se* treatment under the antitrust laws of those individual states

that have their own antitrust statute but do not have a tradition of adhering closely to the precedent of their federal counterparts. In circumstances under state law in which *per se* treatment is a possibility, it may still be relevant to distinguish between restrictions on the licensee's first sale of patented products (more tolerated) and restrictions on subsequent resales (less tolerated). *See, e.g., Lucas Arts Entertainment Co. v. Humongous Entertainment Co.*, 870 F. Supp. 285 (N.D. Cal. 1993).

### ***Exclusive Licensing and Exclusive Dealing***

Exclusive licensing and exclusive dealing, while described in similar terms, actually represent very different arrangements and should be analyzed for antitrust purposes separately. A truly exclusive license is one that restricts the right of the licensor to license others *and* to make use of the licensed technology itself. When the licensor retains the right to make use of the technology, it is more accurate to describe the license as offering "partial" or "limited" exclusivity. An exclusive license is unlikely to raise antitrust issues unless the licensor and the licensee are in a horizontal (or competitive) relationship. Then, the licensing terms would need to be scrutinized to determine whether the parties are allocating the market?a *per se* antitrust offense?through the vehicle of an exclusive license.

In addition, it is important to recognize that licenses that are truly exclusive will be considered "assets" and, therefore, subject to analysis under § 7 of the Clayton Act and possibly reportable under the Hart-Scott-Rodino Act. *See* IP Guidelines § 5.7.

Exclusive dealing occurs with a license, in contrast, when the terms prevent other licensees from licensing, selling, distributing, or using competing technologies. The emphasis of exclusive dealing is on the restrictions the license imposes on the licensee. When evaluating the competitive effects of an exclusive dealing arrangement, the courts and enforcement agencies will consider the market power of the licensor and the degree of foreclosure, among other factors. *See, e.g.,* IP Guidelines § 4.1.2. In more recent cases, exclusivity arrangements with foreclosure percentages as high as 40 percent have been upheld. *See, e.g., Sewell Plastics, Inc. v. Coca Cola Co.*, 720 F. Supp. 1196, 1213 (W.D.N.C. 1989); *United States v. Microsoft Corp.*, 87 F. Supp. 2d 30 (D.D.C. 2000).

### ***Grantbacks***

Grantbacks, which provide that the original licensor has the right on an exclusive or non-exclusive basis to make use of improvements the licensee has made in the licensed technology, are recognized to have potential pro-competitive benefits. The grantback may promote the dissemination of technology by providing assurance to the licensor that it will have a continuing right to make use of its own technology. At the same time, they have the potential to create disincentives on the part of licensees to innovate, and in that respect, grantbacks are potentially anticompetitive. Generally speaking, exclusive grantbacks, in which only the licensor has the right to use the improvements, are far more likely to pose antitrust issues than non-exclusive grantbacks. *See* IP Guidelines § 5.6.

### ***Pooling Arrangements***

Patent pools, which are agreements between two or more patent holders to license one another or third parties, are the subject of considerable guidance from the enforcement agencies, particularly in the several DOJ business review letters, and the courts. *See, supra*, at 4-5. They have the recognized pro-competitive benefits of integrating complementary intellectual property, reducing



transaction costs, disseminating technology, and avoiding litigation. At the same time, patent pools amount to horizontal arrangements and, therefore, create the risk of unlawful allocation of markets and price fixing.

Several safeguards associated with patent pools will minimize the antitrust risk to the licensors. First, limiting the pools to “essential” patents will help ensure that the patent pool integrates only complementary patent rights. Second, use of a patent expert to evaluate each patent’s “essentiality” to the technical standard will help to avoid inclusion of non-essential patents, that is, those that have practical substitutes. Third, non-exclusive licenses will further reduce the risk that the pool would eliminate competition that would otherwise exist in the absence of the arrangement. Fourth, a provision that the portfolio license will be offered on a non-discriminatory basis will be viewed favorably by the agencies. This is particularly important when, as in the case of the DVD patent pool, the licensors were vertically integrated. In these situations, a provision requiring non-discriminatory licensing helps ensure that the patent pool does not impair downstream competition from non-licensors. *See, e.g., DVD Business Review Letter.*

### **Standard Setting**

The adoption of technical or industry standards, whether or not through formal standard-setting organizations, have a number of potentially pro-competitive benefits. Among them are the following:

- Increase the extent of product compatibility and interoperability;
- Increase the speed of product development and distribution;
- Ease the entry of market participants on a wider scale; and
- Advance the globalization of markets.

At the same time, standard setting has the potential to give rise to anticompetitive effects. For example, intellectual property owners that participate in SSOs may manipulate the process unfairly to acquire market power from their patents. The antitrust risks associated with standard-setting activities, as well as some of the measures implemented by SSOs to minimize risk, are discussed below.

### **De Jure and De Facto Standards**

It is important to distinguish between the two general types of standards? *de jure* and *de facto*? when evaluating the potential antitrust issues that might arise from them.

A *de jure* standard is generally one that is adopted by a group following procedures set forth by a trade association or some other formal standard-setting organization. Standard-setting activities by a SSO, depending on the circumstances, are subject to antitrust review under either a *per se* or a rule of reason analysis. *See, e.g., Int’l Ass’n of Conference Interpreters*, 123 F.T.C. 465 (1997) (invalidating the Association’s monetary conditions under a *per se* standard but upholding its working conditions under the rule of reason).

A *de facto* standard is when one industry participant’s proprietary solution becomes so widely or ubiquitously adopted that it is generally used within that industry as a guide to the design of

products.

Both *de jure* standards and *de facto* standards are susceptible to anticompetitive conduct.

### **“Patent Ambush” and “Patent Hold-Up”**

SSOs are susceptible to so-called patent ambush, which consists of a patent holder’s misrepresentation about—or at least a failure to disclose—relevant IP during the standard-setting process. This theory of antitrust liability became prominent when the FTC challenged Dell Computer’s conduct as a member of the Video Electronic Standards Association (VESA) in the mid-1990s. According to the FTC complaint, a Dell representative falsely certified to the SSO that it had no applicable patents with respect to the proposed computer “bus” standard. Eight months after the bus standard was adopted and after its use became widespread, Dell claimed that implementing the standard violated its patent rights. The key to the FTC’s complaint was Dell’s alleged interaction with the SSO. Specifically, the FTC claimed that Dell engaged in an unfair method of competition by knowingly violating the disclosure rules of the SSO. The extent of Dell’s disclosure obligations with respect to the SSO was unclear. Nevertheless, under the terms of the consent decree, Dell was prohibited from enforcing its patents against firms making products in compliance with the bus standard.

More recently, the FTC has pursued similar claims of unfair methods of competition in separate proceedings against Rambus (*In the Matter of Rambus Inc.*, Docket No. 9302, Opinion of the Commission (Feb. 5, 2007), *rev’d in part on other grounds*, 522 F.3d 456 (D.C. Cir. 2008) and against Unocal (*Union Oil Co. of Cal.*, FTC Docket No. 9305 (filed March 4, 2003)). Following a remand of the matter to the ALJ, the FTC, and Unocal reached a settlement. The FTC had previously rejected Unocal’s defense that its representations before the California Air Resources Board (CARB) were immune from antitrust liability under the *Noerr-Pennington* doctrine. Again, the crux of the administrative complaints was patent ambush: using fraud and deceit to induce a standard-setting body to adopt a certain technology that the companies had patented or were in the process of patenting. In *Rambus*, the ALJ’s initial decision was in favor of the respondent, but the full Federal Trade Commission reversed. It found that Rambus had actively concealed and withheld information regarding its relevant patents and patent applications that were material to the standard-setting process for SDRAM. The FTC ordered, as a remedy, compulsory licensing of Rambus’s technology at maximum royalty rates set by the enforcement agency. On appeal, the Court of Appeals for the D.C. Circuit reversed, holding that (notwithstanding the deceptive conduct) the SSO’s loss of an opportunity to negotiate more favorable licensing terms from Rambus did not constitute antitrust injury. A different outcome was reached in *Qualcomm Inc. v. Broadcom Corp.*, 548 F.3d 1004 (3d Cir. 2008), in which the Third Circuit held that Qualcomm had a duty to disclose certain patents to the SSO, and that its failure to do so rendered the patents unenforceable against products manufactured in compliance with the SSO’s standards.

### **Disclosure Rules and Ex Ante Licensing Discussions**

Even with full disclosure of applicable proprietary technologies, there is still the potential problem of “patent hold-up.” Once the standard is adopted, there is no guarantee that the patent holder will cooperate with prospective licensees intent on new developing applications in compliance with the standard.

For the problem of patent hold-up, the traditional solution is for the SSO to solicit a so-called

RAND letter during the standard-setting process, that is, a commitment to license all interested parties on reasonable and non-discriminatory terms. But is that sufficient? Once the interested parties get locked in to the adopted standard, the holder of the relevant technology may still send out demand letters accompanied by take-it-or-leave-it license terms.

Some antitrust commentators have proposed that the most effective solution to the problem of patent hold-up is to allow the SSO to invite the submitter of a RAND letter to include a statement of intended license terms or a statement that the royalty will not exceed X amount. *See, e.g., Skitol, "Concerted Buying Power: Its Potential for Addressing the Patent Holdup Problem in Standard Setting," 72 Antitrust L.J. 727, 742-744 (2005)*. The proposal is to encourage?not mandate?disclosure of such information to allow the SSO and its members to be more informed *during* the standard-setting process. That way, RAND would be enforceable as an *ex ante* test. This approach to the problem of patent hold-up raises another concern: that such conduct by a SSO, even if couched in terms of an invitation, would at the same time expose the participants in the standard-setting process to charges of price-fixing or engaging in a buyer's cartel.

Statements by former FTC Chairman Deborah Platt Majoras (Remarks by Deborah Platt Majoras, Chairman, Federal Trade Comm'n, dated Sept. 23, 2005) and the DOJ's business review letters to counsel for VITA and IEEE have nonetheless signaled a recognition by both federal enforcement agencies of the potential pro-competitive benefits of such *ex ante* licensing commitments. The European Commission also appears to be receptive to such *ex ante* arrangements as reflected in its proposed new Horizontal Guidelines.

## **Issues with De Facto Standards**

### ***Lump Sum Licensing Fees***

A *de facto* standard established outside the context of a formal standard-setting organization may not carry with it the same potential for price-fixing. Yet, other licensing fee issues may arise. As alleged in *United States v. Microsoft Corp.*, 56 F.3d 1448 (D.C. Cir. 1995), the holder of the *de facto* standard may attempt to structure its licensing fee to unlawfully exclude rival competition. For example, a lump-sum fee, as was at one time charged to OEMs licensing the Windows product, has the potential to stifle competition from emerging rival platforms, as it creates disincentives for buyers to invest in competing technologies for a portion of their production capacity.

### ***Possible Deception in Interoperability***

Although *de facto* standards, by definition, are not subject to a formal SSO's rule of disclosure, there is still the potential for accusations of deception in the standard-setting process. In *Microsoft*, the software company was held liable under § 2 for having "deceived" software developers into designing Windows-specific programs when they in fact wished to write cross-platform programs, thus allegedly impeding Sun Microsystem's ability to advance Java as a rival platform. More recently, according to the FTC, deception by Intel Corp., Docket No. 9341, in terms of the interoperability of a central processing unit, or CPU, manufactured by its rival AMD formed part of the basis of the administrative complaint, now settled, against the dominant chip supplier.

### ***Attempted Monopolization/Monopoly Leveraging***

It is possible that the holder of a *de facto* standard will attempt to take advantage of its market

power to leverage a favorable position in a secondary market. The government in *Microsoft* alleged that Microsoft attempted to do so in the separate browser market. The D.C. Circuit rejected a “monopoly leveraging” claim, however, that did not establish a dangerous probability of successful monopolization in the secondary market. The US Supreme Court also reinforced the applicability of traditional § 2 principles in *Trinko*, 540 U.S. at 415 n.4 (“To the extent the Court of Appeals dispensed with a requirement that there be a ‘dangerous probability of success’ in monopolizing a second market, it erred [citations omitted]”).

## Patent Settlements

Settlements of patent infringement litigation, like other forms of agreement, have the potential to create antitrust liability under § 1 of the Sherman Act. They can lead to the reduction in competition by merging competing suppliers of goods and services by allocating customers and markets, by extending the life of patents beyond their statutory terms, or by facilitating a price fixing scheme through cross-license provisions.

At the same time, settlements of patent infringement litigation have strong public policies favoring them. There is the general attitude of the courts favoring settlements of intellectual property disputes. *See* IP Guidelines § 5.5 and Example 10 (“Settlements involving cross-licensing of intellectual property rights can be an efficient means to avoid litigation and, in general, courts favor such settlements.”). More specifically, such settlements not only conserve judicial resources and litigation costs but also facilitate the dissemination of intellectual property.

Most of the recent attention in terms of intellectual property settlements has been in the context of pharmaceutical claims. In particular, so-called reverse-payment settlements, in which the brand name pharmaceutical company provides monetary compensation to the generic manufacturer for an agreement to delay or forego marketing its generic product, has been challenged by both governmental and private litigants as anticompetitive. These settlements are referred to as “reverse-payment” settlements, because the payment is contrary to the typical flow from the alleged infringer to the patent holder.

For the most part, the courts have declined to invalidate such IP settlements on antitrust grounds (*In re Tamoxifen Citrate Antitrust Litig.*, 466 F.3d 187 (2d. Cir. 2006); *In re Ciproflaxacin Hydrochloride Antitrust Litig.*, 544 F.3d 1323 (Fed. Cir. 2008), *cert. denied* 129 S. Ct. 2828 (2009); *Schering Plough Corp. v. Fed. Trade Comm’n*, 402 F.3d 1056 (11th Cir. 2005). On April 29, 2010, a panel of the Second Circuit invited *en banc* review of the issue in another reverse-payment Cipro case, *Arkansas Carpenters Health and Welfare Fund v. Bayer A.G.*, Nos. 05-2851-cv(L) and 05-2852-cv(CON)). A finding of a reverse-payment, while contrary to the usual flow of monetary compensation, has not been sufficient to render the agreements anticompetitive in the view of most courts. Instead, courts tend to look to whether the settlement restricts competition either by extending the life of the patent beyond its statutory life or the scope of its exclusionary rights. In a different context, the DOJ objected to the settlement of the *Google Book* case on the basis that it would extend to the company a monopoly on the commercializing and publishing of millions of out-of-print books. *See* Statement of Interest of United States Regarding Proposed Class Settlement, *The Authors Guild, Inc. v. Google, Inc.*, No. 05-civ-8136 (S.D.N.Y. Sept. 18, 2009). Undeterred by these decisions, the Federal Trade Commission has continued to advocate for restrictions on such settlements, either through enforcement actions or legislation (Jon Leibowitz, Comm’r, Federal Trade Commission, “[Exclusion Payments to Settle Pharmaceutical Patent Cases: They’re B-a-a-a-ck!](#),” Remarks at the Second Annual In-House Counsel’s Forum on

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Pharmaceutical Antitrust at 1 (April 24, 2006).

### Questions to Ask

The following are some (non-exhaustive) questions owners of intellectual property, in conjunction with their counsel, may wish to ask when evaluating the antitrust risks associated with the terms and conditions of a licensing agreement.

1. What is the business purpose of any restraint in the licensing agreement? An IP owner that is unable to articulate a good business reason for a restraint, without looking to counsel for advice, may be raising a red-flag.
2. Are the rights being licensed on an exclusive basis in at least one relevant geographic market or for one particular field of use such that the license amounts to an acquisition that may be reportable under the Hart-Scott-Rodino Act?
3. Is the license agreement between separate economic units such that it meets the “concerted action” element of § 1 of the Sherman Act? A truly intra-company transfer of technology (*e.g.*, between a parent and a wholly owned subsidiary) may not be subject to the antitrust analysis applicable to a license agreement between unaffiliated companies.
4. What is the competitive relationship between the licensor and the licensee? Is it a vertical one or a horizontal one, which tends to raise greater antitrust concerns?
5. Does the licensing agreement amount to a change in policy by the licensor with respect to the intellectual property? As in *Kodak*, a change in policy for distributing intellectual property may be treated less differentially by the courts and the agencies.
6. Does the licensing agreement have a substantial negative impact on any third parties? While the affirmative answer to that question does not mean there will necessarily be any private litigation, just as a negative response does not foreclose the possibility of such litigation, it does amount to a practical consideration in evaluating antitrust risk.
7. What substitutes exist for the licensor’s technology or for the goods and services dependent on that technology? Generally speaking, the fewer substitutes that exist, the more market power the IP owner is likely to possess.
8. Are there substantial barriers to entry in terms of providing technology that would compete with that of the licensor? Again, generally speaking, the more barriers to entry, the more market power the IP owner is likely to possess.
9. Can the IP owner still serve its legitimate purpose with a less restrictive license? This should be evaluated from a practical standpoint. An IP owner need not abandon a licensing provision simply because there is theoretically a less restrictive alternative.
10. Do any of the provisions in the licensing agreement create any natural disincentives to innovate such that competition in a relevant technology or innovation market might be adversely affected?

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