

Antitrust principles applicable to intellectual property

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In 1995, the US antitrust enforcement agencies – the Antitrust Division of the US Department of Justice (DoJ) and the Federal Trade Commission (FTC) (together, ‘the Agencies’) – released their Antitrust Guidelines for the Licensing of Intellectual Property (‘the IP Guidelines’). The IP Guidelines state the Agencies’ enforcement policies when intellectual property is involved. Recently, the Agencies held extensive hearings on ‘Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy’. At these hearings, Charles James (then-Assistant Attorney General, Antitrust Division, DoJ) and Timothy Muris (Chairman, FTC) restated their confidence in the IP Guidelines as providing a framework for evaluating situations where antitrust law and intellectual property law converge. In this chapter, we outline the analysis of conduct involving intellectual property rights under the US antitrust laws and describe situations in which the assertion of intellectual property rights may give rise to an antitrust violation.

Framework for the analysis of use of intellectual property rights under US antitrust laws

The IP Guidelines state three general principles for applying antitrust law principles to intellectual property. First, ‘the Agencies regard intellectual property as being essentially comparable to any other form of property.’ Second, ‘the Agencies do not presume that intellectual property creates market power in the antitrust context.’ Third, ‘the Agencies recognise that intellectual property licensing allows firms to combine complementary factors of production and is generally pro-competitive.’ IP Guidelines § 2.0. With these principles in mind, the IP Guidelines apply ‘the same general antitrust principles to conduct involving intellectual property that they apply to conduct involving any other form of tangible or intangible property’. Id. § 2.1.

The US antitrust laws consist of several key statutes that, over the years, have been interpreted by the courts. When intellectual property is involved, the most relevant statutes are Sections 1 and 2 of the Sherman Act and Section 5 of the FTC Act. Section 1 of the Sherman Act prohibits agreements between two or more unrelated entities that unreasonably restrain trade. See 15 USC § 1. Section 2 of the Sherman Act, 15 USC § 2, prohibits the wilful acquisition or maintenance of a monopoly (or attempt to do so), as distinguished from growth or development ‘as a consequence of superior product, business acumen, or historical accident’. *United States v Grinnell Corp*, 384 US 563, 570-71 (1966). Section 5 of the FTC Act empowers the FTC to challenge ‘unfair methods of competition’. With the exception of the FTC Act, which is enforced only by the FTC, the US antitrust laws are enforced by the DoJ, which has criminal and civil enforcement powers, the FTC, and private entities, which can sue in civil court and potentially recover treble damages and attorney’s fees.

Under the US antitrust laws, conduct is evaluated under the per se rule or the ‘rule of reason’, depending on the conduct. Courts have found conduct per se unlawful (presumed anti-competitive) where licensing of intellectual property was really a pretext for a market allocation scheme, or when an intellectual property holder

tied the sale of one product to the sale of a product protected by an intellectual property right. But, the vast majority of antitrust cases in which intellectual property is involved have been analysed under the ‘rule of reason’. Under the rule of reason, a relevant market is defined and the pro-competitive benefits of the alleged conduct are weighed against the anti-competitive harm. If, on balance, the conduct is pro-competitive, the conduct is lawful.

Relevant market must be defined

When evaluating conduct involving intellectual property under the ‘rule of reason’, the relevant market in which the intellectual property competes must first be defined. A relevant market consists of a relevant product and relevant geographic area. Once defined, the intellectual property holder’s market share is used to assess whether it possesses monopoly or market power. One cannot presume that intellectual property rights confer monopoly or market power on its holder. An intellectual property holder may possess market power if its share of a relevant market exceeds 50 per cent and there are high barriers to entry. The key question for determining the relevant market is whether the product in question has substitutes that customers could economically switch to. If so, these substitutes must be included in the assessment of the relevant market.

Market definition is a threshold issue that may dispose of antitrust cases without any inquiry into the conduct at issue. This principle was recently demonstrated in a case before an Administrative Law Judge at the FTC. In *In re Schering-Plough Corp et al*, No. 9297 (FTC June 27, 2002), the FTC alleged that Schering-Plough engaged in a scheme to suppress competition by delaying the introduction of generic equivalents to its patented drug. The patented drug was a potassium supplement commonly prescribed to patients that also take high blood pressure medication. The case was decided in Schering-Plough’s favour because the FTC’s complaint alleged a relevant market that comprised only the patented drug and its generic equivalents. The court found, however, that the patented drug was one of many potassium products on the market, which greatly diluted Schering-Plough’s market share. Since Schering-Plough’s market share was very low in the proper relevant market, it did not have monopoly power. Thus, the FTC’s case failed because it could not prove an element of its monopolisation claim.

If, on the other hand, an intellectual property-holder possesses monopoly or market power in a relevant antitrust market, then further analysis is required to determine whether its conduct violates the antitrust laws. When intellectual property is involved, certain types of conduct typically are at issue.

Specific areas of application of US antitrust laws to intellectual property rights

Exclusive licensing

An exclusive licence expressly or implicitly restricts the licensor from licensing others. An exclusive licence may raise issues under Section

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1 of the Sherman Act as an agreement that unreasonably restrains trade. An exclusive licence may be horizontal, meaning that the licensor and licensee are actual or potential competitors in the markets covered by the licensed technology. There are some situations where exclusive licences have been found to be per se violations of the antitrust laws. See, eg, *United States v Singer Mfg. Co*, 374 US 174 (1963). This arises when the licence is merely a sham or pretext for a market allocation or price fixing scheme. More commonly, exclusive horizontal licences are evaluated under the rule of reason. Under the rule of reason, if the market is unconcentrated, then the licence is likely to pass antitrust scrutiny. If, however, the market is very concentrated and the licence eliminates a significant competitor, the licence may violate the antitrust laws unless there are significant pro-competitive aspects of the licence.

Vertical exclusive licences are almost always considered lawful under the US antitrust laws. A vertical exclusive licence is between entities that are at different levels of the market. A vertical exclusive licence that contains non-price restrictions is analysed under the rule of reason. An intellectual property holder's right to license its technology is given great deference under the antitrust laws. Only where the vertical licence attempts to set minimum price levels at which the licensee may sell products will the licence attract serious, per se, antitrust scrutiny.

Refusals to license

The essence of the intellectual property holder's rights is the ability to exclude others from using the relevant intellectual property. As mentioned above, the US antitrust laws give great deference to the intellectual property holder's discretion. Indeed, US intellectual property law does not require a holder to use it or license it. A simple refusal to license intellectual property, standing alone, typically cannot form the basis of an antitrust claim. However, recent cases involving monopoly leveraging of intellectual property rights have created some uncertainty on the unfettered rights of intellectual property holders.

In *Image Technical Services Inc v Eastman Kodak Co*, 125 F.3d 1195 (9th Cir. 1997), the Ninth Circuit Court of Appeals held that an intellectual property holder has a presumptive right not to license its intellectual property, unless it has a subjective intent to use these rights to create a monopoly. Under this theory, the following elements must be shown:

- possession of monopoly power in one market;
- refusal to license technology to potential competitors in a second related market,
- with the specific intent to establish a monopoly in the second market.

In direct contrast to *Kodak*, the Federal Circuit Court of Appeals rejected this theory of antitrust liability. In *In re Independent Service Organisations Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000), the Federal Circuit strictly construed an intellectual property holder's right to determine who, if anyone, it wanted to license. In so doing, the Federal Circuit addressed *Kodak* and rejected it as a 'significant departure' from established law. *Id.* at 1329. The Federal Circuit stated that the exercise of patent rights in most cases will not bring antitrust liability for refusals to deal, unless the patent is obtained by fraud, the enforcement litigation is a sham, or the refusal to license is part of an unlawful tying scheme.

Tying

Tying is the conditioning of the sale of one product (the 'tying product') on the buyer's agreement to buy another product (the 'tied product') from the seller. When intellectual property is involved, the tying product is either a licence to technology or to a product that incorporates patented technology. Tying may be analysed under the per se rule or the 'rule of reason'.

A per se tying claim consists of the following elements:

- the tying product and tied product are separate products (or patents);
- the patent holder coerces the licensee to also license the tied product; and
- the licensor/seller has market power in the tying product. Market power is typically the threshold issue.

In *Jefferson Parish Hosp. Dist. No. 2 v Hyde*, 466 US 2 (1984), the Supreme Court opined that the presence of a patent or copyright creates a presumption that market power exists in its holder. However, this notion has been criticised by other federal courts analysing this issue. See, eg, *Abbott Lab. v Brennan*, 952 F.2d 1346 (Fed. Cir. 1991); *American Hoist & Derrick Co v Sowa & Sons*, 752 F.2d 1350 (Fed. Cir. 1984). Moreover, as described above, the Agencies have stated in their IP Guidelines that market power and monopoly power will not be presumed.

A 'rule of reason' tying claim consists of the first two elements of a per se claim, but instead of showing market power, one must show:

- the tying arrangement has an actual anti-competitive effect by reducing competition in the tied product and
- there is no valid business justification.

In *United States v Microsoft*, 253 F.3d 34 (DC Cir. 2001), the DC Circuit held that despite Microsoft's high market share in the computer operating system market, its conduct of bundling a browser with the operating system did not warrant per se treatment as a tying arrangement. Instead, the court remanded for evaluation under the rule of reason because the court did not want to deter innovation that may result from the integration of software products.

Patent pooling

Patent pooling is a form of cross-licensing that involves two or more owners of different patents agreeing to collectively license a set of patents. These arrangements may provide pro-competitive benefits by integrating complementary technologies, reducing transaction costs, clearing blocking positions, and avoiding or settling costly licensing litigation. In analysing a proposed pool, two issues typically must be addressed:

- does the pool formation reduce competition, and
- does the pool's proposed licensing programme restrict or promote competition?

Since a patent pool typically involves an agreement among actual or potential competitors, a threshold issue is whether the rule of reason or per se rule applies. Unless the patent pool is some sort of a sham to fix prices or allocate markets, it will be analysed under the rule of reason. Under the rule of reason, the market for the pooled patents must be assessed to determine if the pool creates market power. Thus, when forming the pool, it must only include those patents that are necessary to produce the relevant product.

When evaluating the legality of the patent pool, it is necessary to analyse the relationship between the pooled patents. If the pool creates market power and the patents are competing patents, then the pool may be anti-competitive. In *In re Summit Technology Inc & VISX Inc*, No. 9286 (FTC March 24, 1998), a cross-licence among companies with competing laser eye surgery technologies was found to eliminate licensing competition between the firms and thus violated Section 1 of the Sherman Act. However, a pool generally will not be presumed anti-competitive if it is limited to blocking or essential patents.

Another important issue in evaluating a patent pools is the effect the

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pool has on innovation. If the pool forces licensees to grant back licences for current or future technology for minimal or no royalties, innovation may be reduced because potential licensees will be disincentivised to engage in research and development to improve pooled patents.

Patent pools typically are considered pro-competitive. A patent pool is an efficient method of promoting the dissemination of technology. Patent pools that integrate complementary technologies, reduce transaction costs by eliminating the need to obtain numerous different licences from multiple patent holders, and clear blocking positions, typically pass antitrust scrutiny. When licensing from a patent pool, the members should not collectively refuse to license their intellectual property, should not refuse to grant a pool licence for purposes of eliminating a competitor, should not use pool licences to allocate markets, and should provide safeguards for licensee's competitively sensitive information.

Exclusive dealing

Exclusive dealing occurs when a licence prevents the licensee from licensing, selling, distributing, or using competing technologies or products incorporating competing technologies. Since exclusive dealing arrangements are vertical in nature, they are evaluated under the rule of reason. In evaluating whether an exclusive dealing arrangement is lawful, the following factors are analysed: the market share of the licensor imposing the exclusive dealing requirement; the degree of foreclosure to suppliers of competing goods or technologies; the duration of the agreement; the likelihood of entry into the market; and the purpose behind the restraint.

Standard setting

Standard setting involves collective industry agreement (a) on the technical or safety requirements for products or (b) to provide for interoperability or compatibility among suppliers of complementary products. Standard setting is often pro-competitive because it can make it easier for products to gain acceptance in the market by giving consumers confidence that products are able to work with one another. Standard setting, however, can raise antitrust concerns if:

- members of the standard setting body use the process to exclude competitors; and
- a member of the standard setting body manipulates the process to monopolise the relevant market.

Under the latter theory, a member of the standard setting organisation convinces the organisation to adopt its product/process as the industry standard. Then the member asserts its intellectual property rights against anyone who uses the standard in products that incorporate the standard. In this situation, the following issues are analysed:

- whether the participant has, or is dangerously close to achieving, monopoly power in the relevant market covered by the technology;
- whether the intellectual property holder failed to disclose its intellectual property to the standard setting body and had a duty to do so;
- whether the conduct is predatory; and
- whether the participant contributes to the adoption of the standard by misrepresentations or omissions.

The FTC recently brought a case against Rambus Inc, alleging violations of the antitrust laws by Rambus in its activities with a standard-setting organisation. See *In re Rambus Inc*, No. 9302 (FTC June 18, 2002). The FTC alleges that Rambus failed to make required disclosures to JEDEC, a standard-setting organisation that develops technical standards for a common type of computer memory. JEDEC standards are incorporated into memory chips that are widely used for various computer products. The FTC has asserted that Rambus reduced competition by failing to disclose its intellectual property when it was required to do so, and then asserted its intellectual property rights over companies that incorporated the standard.

Enforcement of intellectual property rights

There are two situations where enforcement or prosecution of intellectual property rights may give rise to antitrust claims.

Walker Process claims

One issue is whether the intellectual property was obtained by fraud. See *Walker Process v Food Machinery and Chemical Corp.*, 382 US 172 (1965). In asserting a *Walker Process* claim, the following elements must be shown: (i) the patent is invalid; (ii) the defendant made a material misrepresentation or omission to the PTO; (iii) the misrepresentation or omission was made in bad faith; (iv) there was an attempt to enforce the patent by the person having knowledge that



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the patents were invalid; and (v) the other elements of a monopolization or attempted monopolisation claim are satisfied. The Federal Circuit has explained that *Walker Process* claims form an independent legal basis that could potentially strip a patent holder of its 'immunity from the antitrust laws'. *Nobelpharma AB v Implant Innovations Inc*, 141 F.3d 1059, 1071 (Fed. Cir. 1998).

Sham litigation provides another legal theory by which a patent holder may lose its intellectual property rights. *Id.* In order to show a sham: (i) the litigation must be objectively baseless, and (ii) the litigation was filed to use the legal system to harass the defendant and eliminate competition, regardless of the outcome of the litigation. See *Professional Real Estate Investors v Columbia Pictures Industries Inc*, 508 US 49 (1993).

Handgards claims

Efforts to enforce intellectual property rights that were obtained in good faith but that the patentee subsequently learns are invalid may also give rise to an antitrust claim. See *Handgards Inc v Ethicon Inc*, 743 F.2d 1282 (9th Cir. 1984). The elements of a *Handgards* claim are (i) the patentee obtained the patent in good faith; (ii) the patentee subsequently had knowledge that the patent was invalid; (iii) the patentee knowingly sought to enforce the invalid patent; and (iv) the other elements of monopolisation or attempted monopoly are satisfied. This theory may be barred by the Noerr-Pennington doctrine, which exempts efforts to petition for government action such as the filing of a patent infringement suit. The Noerr-Pennington doctrine, however, does not apply if the patent infringement suit is a sham.

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