Antitrust Agencies to Review Relationship of Antitrust Laws and Intellectual Property

Introduction
The Department of Justice (DOJ) and Federal Trade Commission (FTC) have announced that they intend to conduct hearings on the relationship of the antitrust laws and intellectual property this spring. These hearings will explore some of the most interesting and complex questions raised by the intersection of these two bodies of law and are likely to influence the enforcement policy of both agencies. In addition, there is interest in the European Union about how to apply the antitrust laws in this area.

This Client Alert reviews some basic principles regarding the application of antitrust law to intellectual property and discusses some of the cutting-edge issues that are likely to be explored in the hearings: 1) antitrust liability for refusal to license a patent (or what is often the equivalent, refusal to sell a patented product); 2) agreements to settle patent litigation that delay entry of a competitor; and 3) disclosure of intellectual property rights in the standard-setting process.

Companies that frequently license patents or other intellectual property may wish to monitor the hearings or submit a statement on one or more issues.

The Historical Relationship between Antitrust and Patent Law
Antitrust and intellectual property law historically have had a stormy relationship. In the early part of the twentieth century, through perhaps the 1970s, it was customary for courts to view these two bodies of law as separate spheres of the law with incompatible goals. The courts observed that intellectual property creates a legally protected "monopoly," while antitrust seeks to break down monopolies. In case of a conflict between the two, antitrust was generally the winner. Courts frequently found antitrust violations, not because there was a significant effect on competition but because the patent holder had "misused" the patent by extending restrictions beyond the patent right itself. During the 1970s, the Department of Justice Antitrust Division announced what came to be called the "Nine No-Nos" regarding patent licensing, which largely adopted this view in the formal enforcement policy of the DOJ.

The Modern Approach
This early approach has now undergone drastic revision. The Reagan Administration's Antitrust Division repudiated the "Nine No-Nos" in 1981. In 1995, the DOJ and FTC issued
guidelines for analyzing many agreements involving the sale of intellectual property rights. The Guidelines shifted from the formalistic approach of asking whether a licensing agreement extended the patent holder’s rights “beyond” the patent, to the more sensible question of whether an agreement has a significant harmful effect on competition. This more flexible approach has permitted much greater freedom in structuring licensing arrangements. “Patent misuse” is still understood to include actions that improperly attempt to expand the patent right, such as illegal tying, collecting royalties on an expired patent, fraudulently procuring a patent, or bringing unjustified infringement litigation. However, patent misuse does not lead automatically to antitrust liability, although it may be relevant in determining whether an antitrust claim can be made.

To take one example of this new approach, consider tying (requiring the licensee to buy some other product) and package licensing (requiring a licensee to license a number of patents together). The “Nine No-Nos” prohibited both practices on the theory that they extend the patent holder’s rights beyond the scope of the patent grant. In addition, the Supreme Court had appeared to condemn both kinds of practices. Under the Guidelines, however, neither practice is viewed as automatically unlawful. A licensor is not assumed to have market power in a product simply because it is subject to intellectual property protection. Even if the licensor does have market power because of the patent, the tie still might be lawful.

Despite the additional flexibility under the Guidelines, it is important to remember that there is no antitrust immunity for agreements to license patents or to sell patented products. In fact, while most licensing arrangements are subject to a rule of reason analysis (i.e., one that turns on competitive effects) some licensing agreements are per se unlawful (i.e., unlawful without regard to competitive effects). For example, assume A and B manufacture competing products with different patents. A and B agree to license each other’s patents on the condition that they sell the competing products in separate geographic areas. This is likely to be viewed as a per se unlawful territorial allocation agreement structured as a cross-licensing agreement.

**Developments in Europe**

While the US antitrust agencies’ hearings will explore broad questions regarding the relationship between antitrust and intellectual property law, a parallel effort is occurring in the European Union. EU rules for IP licensing are now embodied in the Technology Transfer Block Exemption. The EU has just issued an extensive Report acknowledging a certain rigidity in approach:

The TTBE is generally considered overly formalistic and too complex and in addition too narrow in scope. In some cases, by imposing on companies an unnecessary compliance burden and forcing industry into a legal straitjacket, the TTBE may skew enforcement towards over-deterrence, which may have a negative impact on dynamic efficiency.

The Report goes on to say that “In general EC competition policy has placed more limits on the exploitation of IPR rights than US competition policy.” The EU has invited comments on the issues raised by the Report, with a deadline of April 26, 2002. Thus, further reforms to antitrust limitations on use of intellectual property is under consideration in the world’s two leading economies. Firms that rely heavily on IP rights may want to comment in the EU proceeding as well.

**Current Issues in the U.S.**

There are a number of important recent developments involving antitrust and intellectual property, which will be explored in the FTC/DOJ hearings. The approach of the antitrust agencies toward these issues will have considerable significance for structuring agreements and for bringing and settling patent litigation. Below, we discuss three of the most important ones.

**“Simple” Refusal to License**

In general, a simple refusal by a single party to deal with another party is not an antitrust violation, whether or not intellectual property is involved. While the Supreme Court has identified a number of exceptions to this principle, the courts have not yet developed a unified approach to refusals to deal. However, it is possible to say that some of the most important factors are: 1) whether the party refusing to deal has a monopoly
or near-monopoly market share; 2) whether the refusal leads to harm to competition in a market in which both parties compete; and 3) whether there is a legitimate business justification for the refusal. Liability on this basis will be rare. The argument against antitrust liability for refusals to license a patent or refusal to sell a patented product is even stronger because of the basic policy of the patent laws.

Two courts of appeals have recently split on the standard for evaluating refusal to license cases. In Kodak, the Ninth Circuit upheld a jury verdict finding Kodak’s refusal to sell patented parts to companies that serviced its copiers was an antitrust violation. The court reached this result even though Kodak was not found to have engaged in “patent misuse,” such as illegal tying or bringing an improper infringement claim. According to the Ninth Circuit, a monopolist or near-monopolist (Kodak arguably had a 55 percent market share) is presumed to have a valid business justification for refusing to deal. However, this presumption can be rebutted if the jury finds that the justification is a pretext and the real motive was anti-competitive. Thus, the analysis turns on motivation, a notoriously difficult issue for judges and juries.

In contrast, the Federal Circuit recently adopted a position that is much more protective of the patent holder. In CSU v. Xerox, the court upheld a summary judgment decision in favor of the patent holder on facts similar to those in Kodak. It rejected the Ninth Circuit’s approach and declared that there can be no antitrust liability for a refusal to license a patent or sell patented products unless there had been some type of misuse, such as illegal tying, fraud in the procurement of the patent, or sham infringement litigation. This result follows regardless of the intent of the patent holder or the effect on competition. Former FTC Chairman Pitofsky has criticized this standard as shifting the balance between these two areas of the law too far in the direction of intellectual property protection.

The Federal Circuit’s position in CSU would apparently mean that a monopolist cannot violate the antitrust laws by simply refusing to license valid intellectual property, even if the property is said to constitute an “essential facility” and the refusal harms competition. Despite the very important role of the Federal Circuit in determining federal patent law issues, however, this view is not yet the law of the land. In an amicus brief, the DOJ declined to read the CSU opinion that broadly and commented that it would have “serious concerns” if the Federal Circuit had held that a refusal to license a valid patent could never be an antitrust violation except in the case of an illegal tying arrangement. In addition, in an earlier case involving Kodak, the Supreme Court commented that “the Court has held many times that power gained through some natural and legal advantage such as a patent…can give rise to liability if ‘a seller exploits his dominant position in one market to expand his empire into the next.’” The Federal Circuit interpreted this language narrowly by noting that Kodak had not raised its patent rights as a defense, but this distinction may not be persuasive to other courts.

Because of the important role of the Federal Circuit, and the increasing appreciation of the role of patent policy, the trend is probably away from finding liability for simply refusing to share intellectual property. However, patent holders with high market shares who refuse to license or sell patented products still need to be concerned about the possibility that a refusal to license a patent might create market power in a second market and, therefore, raise antitrust concerns. Patent rights should certainly be asserted as one justification for any such refusal.

“Conditional” Refusals to License

Kodak and CSU, discussed above, involved a simple refusal to deal with a customer. In contrast, a “conditional” refusal to deal includes cases where the licensee is required to provide something in return (e.g., a product or another license). Some conditional refusals to deal are obviously unlawful (e.g., a requirement that a competitor charge a particular price in return for a license). Other reciprocity agreements can be analyzed based on general antitrust principles. For example, a refusal to license a patent unless the licensee agrees to use only the licensor’s patent, can generally be analyzed like an exclusive dealing agreement.
Reciprocity agreements involving exchanges of intellectual property present more difficult issues. The FTC’s Intel case dealt with a refusal by Intel to deny technical information to another party that had initiated infringement litigation against Intel.\(^19\) The FTC’s concern was that Intel’s refusal discouraged innovation efforts by potential competitors. The case was settled when Intel agreed not to withhold product or technical information because of an intellectual property dispute. The Commission was careful to qualify this provision by saying that Intel was free to refuse to license its product or information in the first instance. Thus, the case does not suggest a general requirement for a monopolist to license a patent, even one that might be viewed as essential to competition. Moreover, it is not at all clear that the Federal Circuit would agree with the FTC’s approach if a case were presented on similar facts.\(^20\) Nevertheless, the FTC’s approach means that that patent holders with large market shares should consider antitrust issues in structuring a “conditional” refusal to deal, such as conditioning the sharing of intellectual property on obtaining intellectual property in return.

**Agreements to Delay Entry by Generic Drug Manufacturers**

The FTC has shown strong interest in agreements to settle patent litigation that result in preventing a generic drug manufacturer from marketing its product in competition with an innovator’s product. In *Abbott/Geneva*,\(^21\) the Commission challenged an agreement between an innovator drug manufacturer and a generic manufacturer on the grounds that the patent holder had attempted to prevent a generic competitor from entering the market when its own patent expired. The generic manufacturer had filed with the FDA a request for approval of its drug before the innovator’s patent had expired. Since generic companies are frequently subject to patent infringement suits under those circumstances, the Hatch-Waxman Act grants the first generic manufacturer to file such an application a period of 180 days as the exclusive generic manufacturer whose drug can be approved. The patent holder and the generic manufacturer reached an agreement, which did not settle the litigation but provided temporary relief. The agreement provided very large up-front payments to the generic manufacturer and prohibited the generic manufacturer from giving up its 180-day period of exclusivity.

Patent infringement settlements will naturally include some prohibition on the alleged infringer’s ability to market a product, and the *Abbott/Geneva* agreement could have been viewed simply as an equivalent to an agreed-to preliminary injunction. However, the FTC chose to challenge the agreement because of several unique circumstances. First, the large up-front payments far exceeded any damages that the generic manufacturer could have obtained at that time. Second, the practical effect of prohibiting the generic manufacturer from waiving its 180-day exclusive period was that no other generic manufacturer could attempt to obtain approval.\(^22\) Thus, it appeared to the FTC that the parties had structured an agreement that, as a practical matter, allowed the innovator manufacturer to pay the generic manufacturer to keep all competition out of the market for a prolonged period. That, in turn, allowed Abbott to maintain its monopoly in the market for a very popular drug. Legislation has now been introduced to require innovator manufacturers to file these agreements with the FTC.\(^23\)

This case suggests that drug manufacturers, and perhaps other patent holders, should consider whether agreements to settle patent litigation could be viewed as efforts to delay entry of a non-infringing product.

**Disclosure of Intellectual Property in the Standard-Setting Process**

The FTC has shown a continuing interest in the standard-setting process. In 1996, it challenged the failure of a participant in a standard-setting organization to disclose its patent when the organization had agreed that no standard would be adopted that infringed existing patents.\(^24\) In *Dell*, a major industry association formed a committee to developed a design standard for a computer part. Company representatives on the committee were asked to certify in writing that the proposed standard did not infringe on any intellectual property held by their companies. Dell allegedly signed the agreement but failed to disclose its patent. Dell later informed several of the association’s members that implementation of the standard would violate its
patent rights. The FTC took the position that Dell’s actions caused members of the standard-setting committee to rely on its certification, and, by enforcing the patent later, Dell undermined the standard-setting process.

One member of the Commission felt that the FTC’s order could deter firms from participating in standard-setting by placing too great a burden on participating companies to make such disclosures.25 However, the FTC’s order was limited to a situation where the participants had agreed in advance to make such a certification. The FTC did not require such disclosures in the absence of such a certification. One dispute in the Dell case involved the degree to which senior company officials were aware of the standard-setting process and the requirement to make such a disclosure. It is easy to imagine a case where a lower-level employee participates in the standard-setting and agrees to such a certification, without knowing the full extent of the company’s patent rights and without informing others within the company. Consequently, one lesson of Dell is that companies must monitor their employees’ participation in such standard-setting organizations and any such certifications.

Conclusion

There are a number of important recent developments in the application of the antitrust laws to agreements involving intellectual property. The antitrust agencies are clearly interested in reviewing their enforcement policies in this area and will look for opportunities to challenge intellectual property agreements that raise significant competitive issues. Companies frequently involved in licensing their own intellectual property should monitor these developments and consult antitrust counsel in structuring the licensing agreements in any of the categories discussed above. Please contact any of the attorneys listed below if you have questions about a particular transaction or would like to submit a statement to the antitrust agencies for consideration during the hearings.

---

1 See Willard K. Tom and Joshua Newberg, Antitrust and Intellectual Property: From Separate Spheres to Unified Field, 66 Antitrust L.J. 167, 170-175.
3 Abbott B. Lipsky, Jr. (Deputy Assistant Attorney General for Antitrust), Current Antitrust Division Views on Patent Licensing Practices, 50 Antitrust L.J. 515 (1981) (“When one makes the analysis, one finds that the ‘Nine No-Nos,’ as statements of rational economic policy, contain more error than accuracy.”).
6 Guidelines, Part 2.2.
7 The Supreme Court has not yet definitively resolved whether harm to competition should be presumed in a tie where the seller has market power in the tying product. See Jefferson Parish Hospital District No. 2 v. Hyde, 466 U.S. 2 (1984). Compare Justice Stevens’ opinion, id. at 10-13, which would presume such an effect, with Justice O’Connor’s concurring opinion, which would require a showing of competitive harm, id. at 34-43.
8 Known as the “TTBE”; the formal citation is Commission Regulation (EC) 240/96 on the application of Article 81(3) of the Treaty to certain categories of technology transfer agreements, OJ L 031, 9.12.1996.
10 Id., para. 35.
14 203 F.3d 1322 (Fed. Cir. 2000).
16 The Supreme Court has never expressly stated that a refusal to share an “essential facility” is an antitrust violation. An influential court of appeals opinion, which did recognize such a theory, identified four elements: 1) a monopolist controls the “facility” (which could include intellectual property or some other asset); 2) the competitor cannot duplicate the facility; 3) the competitor is denied access; and 4) it is feasible to share the facility. See MCI Commun. Corp. v. AT&T, 708 F.2d 1081 (7th Cir.), cert. denied, 464 U.S. 891 (1983). For a general discussion of the essential facility doctrine, see Abbott B. Lipsky, Jr., and J. Gregory Sidak, Essential Facilities, 51 Stanford L.Rev. 1187 (1999).
17 See Brief of the United States as Amicus Curiae, CSU v. Xerox, Dkt. No. 00-62 (January 2001).
20 See Intergraph Corp. v. Intel Corp., 195 F.3d 1346, 1362 (Fed. Cir. 1999) (“Commercial negotiations to trade patent property rights for other consideration in order to settle a patent dispute is neither tying nor reciprocity in violation of the Sherman Act.…[I]t is not the judicial role to readjust the risks in high-stakes commercial dealings.”
22 Hoechst Marion Roussel, Inc.; Carderm Capital L.P.; and Andrx Corporation, Dkt. 9293 (final consent order, May 11, 2001).
23 See S. 754, introduced by Senator Leahy, April 6, 2001, and H.R. 1530, introduced by Congressman Waxman.
25 See Dissenting Statement of Commissioner Azcuenaga, id. at 632-33 & n. 11, 635-36.