



The American Antitrust Institute

**REQUEST FOR INVESTIGATION  
OF REMBRANDT, INC. FOR ANTICOMPETITIVE  
CONDUCT THAT THREATENS DIGITAL  
TELEVISION CONVERSION**

**American Antitrust Institute  
Petition to the Federal Trade Commission**

Date: March 26, 2008

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## I. INTRODUCTION

The American Antitrust Institute (“AAI”)<sup>1</sup> petitions the Federal Trade Commission to investigate patent holdup conduct by Rembrandt, Inc., a patent licensing company (also known as a non-practicing entity, or “NPE”), under Section 2 of the Sherman Act and Section 5 of the FTC Act with respect to a government-mandated private standard for digital television broadcasting developed by the Advanced Television Systems Committee (ATSC).

In particular, Rembrandt has failed to abide by an obligation established by the ATSC to license on reasonable and nondiscriminatory (RAND) terms certain technology critical to the delivery of digital systems of terrestrial broadcast television. This RAND commitment was central to the Federal Communications Commission’s (“FCC”) adoption of the ATSC standard in establishing the process for the conversion to digital television. Because the entire U.S. television marketplace will convert to digital systems in the next year, the potential consumer harm from this conduct is enormous. Enforcement action is necessary to protect tens of millions of users of digital television devices, device manufacturers and broadcast networks and cable companies from paying excessive equipment prices and licensing fees due to Rembrandt’s exercise or attempted exercise of monopoly power.

Congress has established February 17, 2009 as the deadline for the final transition from an analog to a digital system for terrestrial broadcast television in accordance with the ATSC standard. Communications systems throughout the U.S. have undergone a revolutionary transition in order to implement the ATSC standard. Affected manufacturers, such as digital television, transmission and reception equipment companies, and end-user companies, such as network broadcast and cable companies, have made significant investments in compliance with the federal mandate and are now “locked-in” to ATSC-compliant digital technology.

The impact of the conversion to digital television on consumers will be substantial. In the next year, tens of millions of U.S. households will purchase converter boxes and other equipment so their analog televisions can function with digital transmissions. Numerous government agencies are acting to assist and subsidize millions of consumers with the conversion to digital television.<sup>2</sup>

Yet the success and cost of this conversion is being threatened by Rembrandt, which is engaging in patent holdup by explicitly repudiating its RAND licensing obligation. Rembrandt brought 14 patent infringement suits against the four major television networks, the five major cable systems, and television and equipment manufacturers seeking licensing royalties that will increase the costs of digital television by tens of millions of dollars. Rembrandt is demanding royalties of 0.5% of “all revenues derived from the use of the

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<sup>1</sup> The American Antitrust Institute is an independent Washington-based non-profit education, research, and advocacy organization. Its mission is to increase the role of competition, assure that competition works in the interests of consumers, and challenge abuses of concentrated economic power in the American and world economy. For more information, please see [www.antitrustinstitute.org](http://www.antitrustinstitute.org). This petition has been approved by the AAI Board of Directors. A list of contributors of \$1,000 or more is available on request. The AAI has been particularly active on intellectual property antitrust issues. This petition is based on publicly available information. The primary authors of the petition are David Balto and Richard Wolfram. Mr. Balto and Mr. Wolfram have worked for industry participants in the past.

<sup>2</sup> For information on the government support of the conversion to digital television, see [www.dtv.gov](http://www.dtv.gov).

ATSC standard” – an amount that would dramatically increase the cost of digital television equipment and the cost of digital television generally. All consumers will pay substantially more for digital and terrestrial television services unless this conduct is enjoined.

At issue in this matter is U.S. Patent No. 5,243,627 (the “‘627 patent”), a patent for signal interleaving transmission in digital television. The patent was originally issued to AT&T and, after several assignments of the patent to AT&T spin-offs, ultimately was assigned to Rembrandt, the current owner. Rembrandt claims that the ‘627 technology is essential to practicing the ATSC standard.<sup>3</sup> In the ATSC standards setting process, AT&T committed to license on RAND terms any patent rights claimed to be essential to the ATSC standard to any applicant seeking to implement the ATSC standard. In adopting the ATSC standard, the FCC required that any intellectual property rights should be licensed on RAND terms. The RAND obligation adopted by the ATSC and FCC was crucial to creating a system of conversion to digital television that could not be held hostage by an owner of intellectual property. Rembrandt has repudiated that obligation. It now asserts that the ‘627 patent is essential to the ATSC standard and seeks injunctive relief against the major broadcast networks, cable systems, and equipment manufacturers refusing to acquiesce to exorbitant and discriminatory licensing demands.

The ATSC standard is the critical element in the development of digital television. The FCC mandated the ATSC standard as the exclusive standard for digital television.<sup>4</sup> For over a decade, in reliance on the ATSC licensing policy and the FCC standard, numerous equipment manufacturers, broadcast networks, cable companies and other industry participants have been designing, manufacturing and selling digital television products and services that implement and practice the ATSC standard. These firms have made substantial investments in ATSC-compliant equipment – including DTV transmitters and demodulators – all in reliance on the ATSC patent policy, the FCC policy, and commitments by ATSC members that licenses to any essential patents would be offered on RAND terms. By its abusive and bad faith enforcement conduct, Rembrandt is undermining the efficient implementation of digital television technology based on the ATSC standard, in accordance with the government’s mandate.

The fact that Rembrandt did not make the original commitment to the ATSC does not relieve it from the RAND obligation. As in the recent FTC enforcement action against N-Data, the same restrictions that applied to the intellectual property of the original owner also apply to its successor.<sup>5</sup> The RAND commitment in question here was made by Rembrandt’s predecessor, AT&T, as a member of the ATSC – presumably in good faith. Rembrandt’s repudiation of the RAND commitment that it assumed upon assignment of the

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<sup>3</sup> As described herein, there is ongoing intellectual property litigation between Rembrandt and other firms about whether certain products infringe the ‘627. Some of the defendants in those cases have taken the position that the technology is not essential to the ATSC standard and that although they are practicing the standard, they are not infringing the ‘627. (The determination in court of whether the patent is infringed and/or essential will likely require several years of litigation and many millions of dollars in defense fees and costs.) Rembrandt asserts that the technology is essential to the ATSC standard and, as explained in further detail below, that assertion should provide a basis for an investigation.

<sup>4</sup> *In Re Advanced Television Systems and their Impact Upon the Existing Television Broadcast Service*, FCC Dkt. No. 87-268, Fourth Report and Order (Dec. 24, 1996) (“FCC Fourth Report and Order”) (*available at* [http://www.fcc.gov/Bureaus/Mass\\_Media/Orders/1996/fcc96493.txt](http://www.fcc.gov/Bureaus/Mass_Media/Orders/1996/fcc96493.txt)).

<sup>5</sup> *In re Negotiated Data Solutions*, FTC File No. 051-0094, Agreement Containing Consent Order (Nov. 9, 2007), Statement of the Commission (Jan. 23, 2008), and Proposed Complaint.

relevant patent rights violates its obligation of good faith and fair dealing to carry out the commitment and has had the effect of distorting competition for the affected transmission technology.

FTC intervention is consistent with the Commission's past enforcement actions in *Unocal*, *Rambus* and *N-Data*. As in those cases, the conduct at issue here harmed competition because it undermined the expectations of the original participants in the standard setting endeavor. If ATSC members had known that AT&T's RAND commitment could be repudiated, they would have been better able to evaluate and compare the cost of licensing and they could have chosen any one of several competing transmission technologies.

Injunctive relief is necessary to stop Rembrandt from engaging in this anticompetitive patent holdup and undermining the implementation of digital television – and time is short because millions of consumers must purchase the necessary equipment in the next year. Such relief is furthermore warranted to establish that in similar situations in the future, where the facts otherwise call for antitrust enforcement, NPEs or any other firms that repudiate SSO RAND commitments to which they have succeeded cannot, as a matter of law, escape antitrust scrutiny simply because they themselves did not engage in inducement of the choice of their predecessor's technology for the standard. And in these circumstances Commission action requires a lower threshold of proof than private treble damages actions.<sup>6</sup>

Consumers here will not necessarily be protected from higher prices or other harm by any private remedies that the broadcast networks, cable companies, television and equipment manufacturers might ultimately obtain in defending ongoing patent litigation with Rembrandt (described in detail below). The defendants in those cases may ultimately prevail, but such litigation is costly, time-consuming and uncertain. Moreover, the ultimate cost of the resolution may be borne by consumers. As a general matter, it has been noted that “when a standard used in a fairly competitive industry is subject to *uniform* hold-up [as here, and as distinguished from hold-up of a single firm], direct buyers may bear little of the costs, which falls primarily on final consumers.”<sup>7</sup> In short, the remedies sought or ultimately accepted by defendants in the pending infringement litigation will not necessarily protect ultimate consumers from higher prices or other harm.

In sum, FTC investigation and enforcement is necessary to prevent tens of millions of consumers from higher prices and protecting the process of the conversion to digital television.

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<sup>6</sup> See, e.g., Areeda and Hovenkamp, *Antitrust Law*, ¶¶ 651b, 337b (generally) (2006).

<sup>7</sup> J. Farrell, J. Hayes, C. Shapiro and T. Sullivan, “Standard Setting, Patents, and Hold-Up,” 74 *Antitrust L.J.* 603, 645 (Issue 3, 2007). As the authors explain, the reason for this is that “[i]f each direct buyer knows that its rivals are paying as high a royalty as it is, pass-through can largely immunize it against economic loss from high running royalties. Thus, the direct buyers, who might otherwise be the best guardians against gratuitous insertion of patents in standards, or against excessive royalties from such patents, may bear very little of the harm. [. . .] Thus, consumers are not, in general well protected by the self-interest of direct technology buyers.” *Id.*

## II. FACTS

Rembrandt Technology LP is a limited partnership organized and existing under the laws of New Jersey with a principal place of business in Bala Cynwyd, Pennsylvania. Rembrandt is a patent holding and licensing company whose principal purpose and activity is to acquire patents and pursue and secure revenue from such patents, and it does not manufacture or sell any products.

### The Conduct at Issue

The facts leading up to Rembrandt's alleged exclusionary conduct and illegal monopolization follow three converging lines of developments in communications transmission technology, manufacturing and standardization, dating back at least since 1987. One trajectory begins with the issuance of the patent at issue in this matter to AT&T Bell and follows its multiple assignments, ultimately to Rembrandt. The second trajectory is the development and adoption of a digital television standard by the Advanced Television Systems Committee (ATSC), a private standard setting organization in which AT&T Bell was a significant participant. The third trajectory was an eight-year Federal Communications Commission proceeding regarding advanced television systems, which concluded with the FCC mandating the adoption of the ATSC standard as the exclusive standard for digital television (DTV).

These three trajectories have converged in Rembrandt's denial that it has any ATSC RAND obligation with respect to the patent at issue, its refusal to license any manufacturer on RAND terms, and its initiation of numerous patent infringement actions seeking injunctions against, and corresponding royalty demands from, various end-users – broadcast networks and cable companies in particular – based on their revenues from ATSC-compliant digital transmission, which Rembrandt claims infringes the '627 patent.

**(1) The patent trail:** U.S. Patent No. 5,243,627 describes a technology for signal interleaving transmission used in television (the "'627"). The application for the '627 was filed with the U.S. Patent and Trademark Office in August 1991. The inventors assigned their rights in the pending patent to American Telephone and Telegraph Company ("AT&T Bell") and the patent issued on September 7, 1993. AT&T Bell changed its name to AT&T Corp. in 1994. AT&T spun off Lucent Technologies Inc. and assigned the '627 to Lucent in March 1996. Lucent subsequently spun off AT&T Paradyne Corp. ("Paradyne") and assigned the '627 to Paradyne in July 1996. Finally, on December 10, 2004, Paradyne assigned the '627 to Rembrandt.

**(2) Adoption of a DTV standard by the ATSC:** Concurrently, in May 1993, seven companies and institutions, including AT&T Bell, joined together in what became known as the "Grand Alliance" to work cooperatively as members of and under the auspices of the ATSC to develop a final digital ATV system and standard based on that system. The ATSC, a private standard setting organization organized according to the policies of the American National Standards Institute (ANSI), was comprised of representatives of major segments of widely divergent industries engaged in telecommunications-related work.

The Grand Alliance was formed from the four winners of a contest sponsored by the FCC to determine the best standard for high-definition television. The four winning systems were designed by AT&T/Zenith, General Instruments/MIT (responsible for two systems) and Philips/Thomson/Sarnoff Research Center. The Grand Alliance members had funded an independent testing facility, the Advanced Television Testing Center, which conducted multiple arm's-length tests and continuously suggested areas for improvement. The FCC was unable to choose from among the four systems and thus charged the Grand Alliance with the task of negotiating and selecting a best-of-breed system, choosing technologies and methods for transmission, image, sound and so forth. They were to integrate the best technologies from each winning system into a single system that would then be the standard. Several companies vied for selection of their RF transmission modulation technology for inclusion in the standard. Among the technologies competing for the RF modulation portion of the standard was a QAM transmission technology employed by General Instruments (later acquired by Motorola). This QAM technology lost out to Zenith's 8 level vestigial sideband (8VSB) modulation system, which Rembrandt claims uses AT&T's signal interleaving method as part of the forward error correction coding.

The Grand Alliance engaged in development and testing for nearly three years, beginning in 1993 and culminating in the ATSC's adoption of a digital television broadcasting standard with the publication on September 16, 1995 of the ATSC A-53 Digital Television Standard (the "ATSC DTV standard" or "ATSC standard"). With respect to digital transmission, the ATSC standard incorporated modulation and transmission exciter technology, which Rembrandt asserts utilizes the '627 patent. The ATSC standard was "voluntary," like many other standards, in the sense that it was adopted by private parties under the auspices of a private SSO.

AT&T, as a condition of its participation in the development and adoption of the standard, was required to agree, and did agree, to an ATSC Patent Policy issued in 1986.<sup>8</sup> The ATSC Patent Policy required that all ATSC participants license either without compensation or on reasonable and non-discriminatory (RAND) terms any invention whose use would be required for compliance with the proposed ATSC Standard.<sup>9</sup> By letter dated January 12, 1995 and addressed to the ATSC, AT&T IPM Corp., a wholly owned subsidiary of AT&T Corp.,<sup>10</sup> committed to "license [its] patents which relate to the ATSC Standard for HDTV, to the extent that the claims of such patents are directed toward and are essential to

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<sup>8</sup> The ATSC Patent Policy is dated Dec. 1, 1986 (the "1986 Patent Policy").

<sup>9</sup> *Id.* at ¶ 2. A later version of the 1986 Patent Policy, updated as of Dec. 6, 2004, (the "2004 Patent Policy"), states that "It shall be the policy of the [ATSC] that Essential Claims included in ATSC Specification Documents be available to implementers on reasonable and non-discriminatory terms." The 2004 Patent Policy defines "Essential Claims" as "claims of all patents issued, and patent applications filed, under the laws of any country that are necessarily infringed by implementing the normative portion of a Specification Document [i.e., ATSC standard]." Both versions of the Patent Policy make it clear, however, that in publishing the ATSC standard, "no position is taken with respect to the validity of [any] claim or of any patent rights in connection therewith." See 1986 Patent Policy at ¶ 2 and 2004 Patent Policy at ¶ 2.

Also, pursuant to the 2004 Patent Policy, if any participant viewed its patented technology as essential to the ATSC standard but would not agree to license it on RAND terms, then that participant was obligated specifically to identify the technology to the ATSC before the standard specification was voted on so that the SSO could take appropriate steps before adopting the specification. *Id.* at ¶ 1. Furthermore, under the terms of the Patent Policy, any ATSC participant that failed to disclose its refusal to license a potential claim, i.e., a patent that it deems essential to the ATSC standard, was deemed to agree to license any resulting "Essential Claim" on reasonable and non-discriminatory terms to all comers. *Id.* at ¶ 6.

<sup>10</sup> AT&T Bell had changed its name to AT&T IPM in 1994.

the implementation of the Standard.” AT&T IPM further committed to grant such licenses “under reasonable terms and conditions on a non-discriminatory, non-exclusive basis.” Further evidencing AT&T’s intent and understanding with respect to ATSC participants’ licensing obligations – and well pre-dating the January 1995 letter commitment – in 1993 an AT&T executive testified before a House subcommittee that “[w]hatever standard is adopted by the FCC, the technology behind it will be required to be licensed to anyone on reasonable terms.”<sup>11</sup>

**(3) FCC proceeding and adoption of the ATSC standard:** In 1987 the FCC commenced a formal proceeding relating to the introduction of advanced television (ATV) and established an Advisory Committee on Advanced Television Communications (ACATS) to provide recommendations on technical, economic and public policy issues. The proceeding is explained in and was formally concluded by a report and order in 1996 adopting the ATSC DTV standard (“FCC Fourth Report and Order”).<sup>12</sup>

On December 24, 1996, just three months after the ATSC had published its DTV standard, and based on a formal recommendation by the ACATS, the FCC issued the Fourth Report and Order, mandating the adoption of the ATSC DTV standard as the sole standard for digital television broadcasting.<sup>13</sup> The legal and practical competitive import of this FCC mandate was to require use of the once-voluntary ATSC standard as the exclusive, government-mandated standard for digital television transmission, thereby precluding any competing standard or any competing or different non-ATSC-compliant technology.<sup>14</sup> The ATSC standard is thus the established, mandatory standard for digital television broadcasting throughout the U.S.

The FCC’s adoption of the ATSC standard in the Fourth Report and Order was explicitly conditioned upon all ATSC participants’ agreeing to license on RAND terms, to *other manufacturing companies*, technology that the participants deemed relevant to the standard. Thus, the FCC stated:

In earlier phases of this proceeding we indicated that, in order for DTV to be successfully implemented, *the patents on the technology would have to be licensed to other manufacturing companies on reasonable and nondiscriminatory terms*. We noted that the system proponents that participated in the Advisory Committee’s competitive testing process were required to submit a statement that they would comply with the ANSI patent policies. The proponents agreed to make any relevant patents that they owned available either free of charge or on a

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<sup>11</sup> Statement of Robert Graves, AT&T Vice President, Video Technology, before the Subcommittee on Telecommunications and Finance, U.S. House of Representatives, May 27, 1993.

<sup>12</sup> *In Re Advanced Television Systems and their Impact Upon the Existing Television Broadcast Service*, FCC Dkt. No. 87-268, Fourth Report and Order (Dec. 24, 1996) (“FCC Fourth Report and Order”) (*available at* [http://www.fcc.gov/Bureaus/Mass\\_Media/Orders/1996/fcc96493.txt](http://www.fcc.gov/Bureaus/Mass_Media/Orders/1996/fcc96493.txt)). As the proceeding progressed, the FCC began to refer to ATV as digital television (DTV) as a reflection of the Commission’s certainty that any ATV system would be digital.

<sup>13</sup> See Fourth Report and Order at § 4 et seq. regarding historical background.

<sup>14</sup> See *id.* at Appendix A, amending the FCC’s Rules and Regulations (47 CFR, Chapter I) to add a new Section 73.682(d) as follows: “73.682 -- TV transmission standards: (d) Digital broadcast television transmission standard. Transmission of digital broadcast television (DTV) *shall comply* with the standards for such transmissions set forth in ATSC Doc. A/53 (“ATSC Digital Television Standard, 16 Sep 95”) [i.e., the ATSC standard] . . . .” (Emphasis added).



reasonable nondiscriminatory basis and we stated that we intended to condition selection of a DTV system on such commitments. [ . . . ]

We reiterate that *adoption of this standard is premised on reasonable and nondiscriminatory licensing of relevant patents.*<sup>15</sup>

***The three trajectories have now converged.*** Based on the ATSC commitment and the FCC policy manufacturers, broadcast networks and cable networks made significant investments based on the ATSC standard. Soon after it acquired the rights to the '627 patent, Rembrandt unequivocally denied that it has – or that AT&T ever had – any RAND commitment to the ATSC, refused to license on RAND terms, and began pursuing extensive litigation in which it alleges that various end-users, including cable companies and the broadcast networks, are infringing the '627, demanding royalties from such end-users based on their total digital television revenues.

- ***Infringement Litigation.*** Beginning in September 2005, with the filing of an infringement suit against Comcast Corporation, Rembrandt has commenced some 14 patent infringement actions against broadcast networks and cable companies and one manufacturer. Rembrandt has sued the four major networks – CBS, NBC, ABC and Fox – (in Delaware federal district court), cable companies Cablevision (in the District of Delaware), Adelphia (Southern District of New York) and Comcast, Charter Communications, Time Warner Cable and Comcast (Eastern District of Texas), and digital television manufacturer Sharp Corporation (Eastern District of Texas). Each of the suits alleges, *inter alia*, that compliance with the ATSC standard relating to cable modems and equipment and the receipt and transmission of certain digital broadcast signals necessarily infringes the '627. On June 21, 2007, the suits were consolidated for pre-trial multi-district litigation proceedings in the District of Delaware.<sup>16</sup>

- ***Letters to Broadcast Networks.*** On February 15, 2007, Rembrandt wrote identical letters to the four major networks, stating that the '627 is “directed toward and essential to the implementation of the Standard” and proposing to license the '627 for “a license fee of one-half percent (0.5%) of all revenues derived from use of the ATSC standard

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<sup>15</sup> Fourth Report and Order at ¶ 54-55 (emphasis added). Central to the FCC proceeding concluding in the government's mandating the ATSC standard were questions over the need for and wisdom of a federally mandated rather than entirely market-driven standard for digital television transmission. The FCC received a wide range of comments from broadcasters, equipment manufacturers, consumer groups, and cable and computer interests, about “whether and how to adopt technical standards for digital broadcast and the proper role of government in the standard setting process.” Fourth Report and Order at ¶ 8. There was widespread agreement among these diverse interests that DTV is particularly characterized by network effects, i.e., the increased benefits that accrue to other DTV users when any particular user adopts DTV. There was some disagreement, however, especially from cable and computer interests, over the severity of potential problems relating to “startup” (i.e., everyone would be better off adopting DTV technology but no one has the incentive to move first), “coordination” (the collaborative effort by broadcasters, consumer equipment manufacturers and program producers that is necessary to introduce DTV), and “splintering” (a breakdown of the consensus or agreement to use the DTV standard). Fourth Report and Order at ¶¶ 8-18. Indeed, implicit throughout the Fourth Report and Order was the possibility that the proceeding need not have concluded in a federally mandated standard. The FCC was concerned that market solutions would yield manifold increased inefficiencies through the adoption of more than one sustainable transmission standard. In the FCC's view, a market solution, instead of one, federally mandated standard, would result in continuing competition among different, incompatible standards, causing harm to consumers and creating greater obstacles to preserving a universally available broadcast television service; could cause some consumers and licensees to postpone purchasing DTV equipment, thereby slowing investment and the transition to DTV; and make it more difficult to facilitate an efficient allotment of broadcast channels and protect against interference. *Id.* at ¶¶ 34-37.

<sup>16</sup> *In re Rembrandt Technologies LP Patent Litigation*, MDL 1848 (D. Del.).

by your company as a broadcaster licensee.”<sup>17</sup> Similarly, on or about the same date, Rembrandt sent a letter to one or more cable companies that were substantially identical to the letters to the networks except in the wording of the license proposal: here, Rembrandt proposed “to license the ‘627 for a license fee of one-half percent (0.5%) of all revenues your company derives from use of the ATSC standard for digital broadcast over a cable network by your company as an MSO [Multi-System Operator] licensee.”<sup>18</sup>

- ***Litigation with Harris.*** Harris is a manufacturer of digital transmission devices. Faced with Rembrandt’s refusal to license the ‘627 on RAND terms, Harris filed suit in May 2007 in federal district court in Florida against Rembrandt for breach of contract.<sup>19</sup> Rembrandt moved to dismiss on the theory that the ATSC patent policy and AT&T IPM’s RAND letter did not create an enforceable contract, and also for lack of personal jurisdiction. In September 2007, the court granted the motion for lack of personal jurisdiction, without addressing Rembrandt’s argument on the contract. On the same day as the dismissal in Florida, Rembrandt filed a declaratory judgment action against Harris in Delaware state court for non-breach of any contract with Harris.<sup>20</sup> Rembrandt asserts in the complaint that “[n]one of AT&T’s or AT&T IPM’s actions with regard to the ATSC standard or ATSC patent policy created a contractual right or other right, directly or as third party beneficiaries, between AT&T and Harris or Harris’ customers to license the ‘627 patent.”<sup>21</sup>

### III. LEGAL ANALYSIS

#### A. Overview of Rembrandt’s Patent Hold-Up.

Standard setting is a cooperative process designed to ensure open competition for the standard. It can trigger the application of antitrust and unfair competition law because it leaves room for distortion of that competition through deception or other bad faith conduct, with anticompetitive effects.<sup>22</sup> Standard setting supplants market competition with a process of controlled competition for a standard. The success of this process depends on good faith adherence by standard setting participants to obligations designed to prevent the acquisition or exercise of market power otherwise conferred by the choice of a standard.<sup>23</sup> SSO obligations typically require ex ante disclosure of proprietary technology essential to the standard and a commitment to RAND licensing.<sup>24</sup> The failure to abide by these rules creates the potential for competitive harm through distortion of competition for the

<sup>17</sup> Identical letters dated February 15, 2007 from John Garland, Rembrandt, to ABC, CBS, NBC and Fox.

<sup>18</sup> *Id.*

<sup>19</sup> *Harris Corp. v. Rembrandt Technologies, L.P.*, 6:07-CV-796-ORL-18DAB (Middle Dist., Fl., Orlando Div.) (Motion to Dismiss filed Aug. 17, 2007) (dismissed for lack of personal jurisdiction on September 21, 2007).

<sup>20</sup> *Rembrandt, Inc. v. Harris Corp.*, Civ. No. 07C-09-59, New Castle Sup. Ct., Del. (Complaint filed Sept. 21, 2007).

<sup>21</sup> *Id.*, Complaint, ¶ 8 (emphasis added).

<sup>22</sup> As the Supreme Court commented in *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 505-06 (1988), “private standard setting” is “the type of commercial activity that has traditionally had its validity determined by the antitrust laws themselves” and “private standard-setting by associations comprising firms with horizontal and vertical business relations is permitted at all under the antitrust laws only on the understanding that it will be conducted in a nonpartisan manner offering procompetitive benefits . . . .”

<sup>23</sup> An implied duty of good faith arises from any joint undertaking such as cooperative standard setting. *See, e.g., Agere Systems Guardian Corp. v. Proxim, Inc.*, 190 F. Supp.2d 726, 738-39 (D. Del. 2002) (allowing pleading of counterclaim for breach of implied duty of good faith and fair dealing against patent holder that sued user of industry standard for infringement based on patent not disclosed in standard setting process).

<sup>24</sup> *See, e.g.,* M. Lemley, “Intellectual Property Rights and Standard-setting Organizations,” 90 Calif. L.Rev. 1889, 1904-06 (Dec. 2002); *see also* M. Naughton and R. Wolfram, “The antitrust risks of unilateral conduct in standard setting, in the light of the FTC’s case against Rambus Inc.,” 49 The Antitrust Bulletin, No. 3, 699, 702, 759-770 (typical search, disclosure and licensing rules) (Fall 2004).

standard. This ultimately undermines firms' incentives to participate in standard setting, thereby depriving society of the procompetitive benefits that standardization can yield.

Disclosure of patent positions and licensing terms (at least to the extent of making a RAND commitment) is particularly important in view of the ensuing phenomenon of lock-in, which occurs after the adoption of the standard. Before a standard is adopted, multiple technologies may compete to be included in the standard and SSO participants typically can switch relatively easily among them. But once a particular standard has been chosen and products have been developed based on that standard, and the market has accepted the standard, it can be extremely expensive (due to high switching costs) or even impossible as a practical matter to substitute one technology for another. Industry participants therefore become locked in to the standard.<sup>25</sup> Of course, if there is one, federally-mandated standard, then only technology compliant with that standard is permitted – as in the case of the ATSC standard.

These principles apply fully to the facts set forth here. Rembrandt has engaged in exclusionary patent 'hold-up' and monopolized the technology market for digital television RF transmission modulation technology by repudiating the RAND commitment, first made by AT&T IPM and ultimately assumed by Rembrandt, to license the '627 technology on RAND terms.<sup>26</sup> The FCC's adoption of the ATSC standard as a mandatory government standard was explicitly conditioned on the RAND commitments of all of the ATSC members. Adherence to these commitments is critical to precluding exclusionary exploitation of the additional power that was otherwise conferred when proprietary technology was included in the ATSC standard. Without this protection in place, a participant, or its successor can gain monopoly power by exacting prohibitively expensive and/or discriminatory royalties, in contravention of the other SSO participants' reasonable expectations, and to the detriment of alternative technologies that competed for the standard.

In short, Rembrandt's refusal to license on RAND terms constitutes exclusionary patent hold-up. Rembrandt has thereby willfully obtained – or at least has a dangerous probability of achieving – monopoly power that it would not otherwise possess.

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<sup>25</sup> See, e.g., Federal Trade Commission, *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy*, Ch. 2 at 29 (2003). See also David J. Teece and Edward F. Sherry, "Standard Setting and Antitrust," 87 *Minn. L.Rev.* 1913, 1917, 1918 (2003) (explaining lock-in and switching costs as a function of sunk costs, the need for compatibility and the difficulty of coordination among firms for switching).

Summarizing this process, the DOJ-FTC 2007 Intellectual Property Report explains that before an SSO chooses a standard, "multiple technologies may compete to be incorporated into the standard under consideration." U.S. Department of Justice and Federal Trade Commission, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (April 2007) at 35-36 ("DOJ/FTC Intellectual Property Report"). But, "[o]nce a technology has been selected and the standard that incorporates the technology has been specified, however, the standard's adopters often will face significant relative costs in switching to an alternative standard." *In the Matter of Negotiated Data Solutions LLC*, FTC File No. 0510094 (Dissenting Statement of Chairman Majoras) (Jan. 23, 2008) (explaining principles behind antitrust 'hold-up' cases). Thus, "[a]fterwards, or ex post, the chosen technology may lack effective substitutes precisely because the SSO chose it as the standard. Thus, ex post, the owner of a patented technology necessary to implement the standard may have the power to extract higher royalties or other licensing terms that reflect the absence of competitive alternatives. Consumers of the products using the standard would be harmed if those higher royalties were passed on in the form of higher prices." DOJ/FTC Intellectual Property Report at 36.

<sup>26</sup> Implied in this commitment was an obligation of good faith, which the FTC found to have been violated in *Rambus*. See also fn. 23, *supra*.

Rembrandt's conduct not only distorted competition for the standard but is now harming manufacturers, cable companies and broadcast networks, and also (prospectively) all television viewers, through higher costs and increased uncertainty regarding compatibility with the standard. Taken as a whole, Rembrandt's conduct threatens to undermine the efficient introduction of DTV by the federally mandated date of February 17, 2009 and, more generally, undermines the efficiencies that collaborative standard setting is intended to achieve.

We turn now to a discussion of the following core claims: (i) Rembrandt succeeded to AT&T's RAND commitment; (ii) Rembrandt's conduct constitutes monopolization or at least attempted monopolization under Section 2; (iii) the conduct constitutes a violation of Section 5 as an unfair method of competition and unfair act or practice; and (iv) the conduct is threatening harm to competition and antitrust injury to consumers.

### **B. Rembrandt Succeeded to AT&T's RAND Commitment.**

First, we address the predicate question of successor obligation – that is, why Rembrandt should be deemed bound to the RAND commitment. Rembrandt assumed the obligations of AT&T IPM with respect to the ATSC upon the assignment of the '627 by Paradyne to Rembrandt on December 24, 1994.<sup>27</sup> The RAND commitment followed the patent and Rembrandt thus had at least constructive if not actual knowledge of the commitment upon the assignment of the patent. Rembrandt in essence stepped into AT&T IPM's shoes and committed – just like AT&T IPM – to license the '627 on RAND terms.<sup>28</sup>

The FTC recently dealt with a similar set of facts involving successor licensing obligations in *In re Negotiated Data Solutions ("N-Data")*.<sup>29</sup> The Commission found that the respondent, N-Data, a patent licensing company – i.e., non-practicing entity ("NPE") – violated Section 5 of the Federal Trade Commission Act by renegeing on a 1994 letter commitment by National Semiconductor Corporation to the IEEE, an electronics standard setting organization, to license on specified terms certain patented technology relating to Ethernet, a computer networking standard used in nearly every computer sold in the U.S. In 1997 National had assigned the relevant patents to Vertical Networks, which in turn assigned them to N-Data in November 2003. The Commission implicitly predicated its finding of illegality under Section 5 of the FTC Act on the conclusion that upon the assignment to N-Data, N-Data assumed National's licensing commitment.<sup>30</sup>

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<sup>27</sup> See, e.g., *Moldo v. Matsco, Inc. (In re Cybernetic Servs.)*, 252 F.3d 1039 (9<sup>th</sup> Cir. 2001), *cert. denied*, 2002 U.S. LEXIS 683 (2002) (citing *Keystone Type Foundry v. Fastpress Co.*, 272 F. 242, 245 (2d Cir. 1921) ("It had long passed into the textbooks that . . . an assignee acquired title subject to prior licenses of which the assignee must inform himself as best he can at his own risk")); *Worley v. Tobacco Co.*, 104 U.S. 340, 344 (1881) ("The assignee of a patent-right takes it subject to the legal consequences of the previous acts of the patentee."); see also Alice Haemmerli, "Why Doctrine Matters: Patent and Copyright Licensing and the Meaning of Ownership in Federal Context," 30 *Columb. J.L. & Arts* 1, n.247 (Fall 2006) (noting that patents are taken subject to existing licenses); see generally 35 U.S.C. § 261 ("Subject to the provisions of 35 U.S.C. §§ 1 et seq. [the Patent Code], patents shall have the attributes of personal property.")

<sup>28</sup> See, e.g., January 12, 1995 letter from AT&T IPM to ATSC; ATSC Patent Policy .

<sup>29</sup> FTC File No. 051-0094, Agreement Containing Consent Order (Nov. 9, 2007), Statement of the Commission (Jan. 23, 2008), and Proposed Complaint.

<sup>30</sup> The Proposed Complaint alleges, in this regard, simply that "Respondent possessed a copy of, and was familiar with the June 7, 1994 letter of assurance when it received assignment of the Patents from Vertical." Proposed Complaint, ¶ 34.

Based on the common law principle that the assignee of a patent takes subject to any licenses of its assignor<sup>31</sup> and the Commission's *N-Data* action, it is clear that Rembrandt assumed AT&T IPM's RAND licensing commitment to the ATSC, no less than N-Data assumed National's licensing commitment.

**C. Rembrandt's Conduct Constitutes Monopolization  
And Attempted Monopolization under Section 2 of the Sherman Act  
And Unfair Competition Under Section 5 of the FTC Act.**

The FTC's enforcement authority under Section 5 of the FTC Act reaches conduct that violates the Sherman Act.<sup>32</sup> Section 2 of the Sherman Act makes it unlawful to "monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations."<sup>33</sup> Monopolization requires proof that the defendant (1) possesses monopoly power in the relevant market and (2) has acquired, enhanced, or maintained that power by the use of exclusionary conduct.<sup>34</sup> Exclusionary conduct within the meaning of Section 2 is understood to be "the willful acquisition or maintenance of [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."<sup>35</sup> The use of exclusionary conduct to obtain or maintain monopoly power is thus the very opposite of competition on the merits, which the antitrust laws are intended to promote.

Attempted monopolization requires proof that the defendant (1) engaged in exclusionary conduct (the same exclusionary conduct in kind and degree as required for monopolization), (2) with a specific intent to monopolize, and (3) with a "dangerous probability" of achieving monopoly power.<sup>36</sup> Section 5 of the Federal Trade Commission Act (FTC Act) prohibits "unfair methods of competition" and "unfair or deceptive acts or practices."<sup>37</sup>

**1. Monopolization**

Rembrandt has willfully acquired and maintained monopoly power in the technology market for DTV signal interleaving and encoding through exclusionary conduct by claiming the '627 is essential to the ATSC standard and then clearly repudiating and breaching the RAND commitment. Rembrandt's unlawful monopolization is established with proof that (1) Rembrandt engaged in exclusionary conduct, (2) it acquired monopoly power, (3) it did so as a result of exclusionary conduct, and (4) this conduct harmed competition and consumers.

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<sup>31</sup> See fn. 27, *supra*.

<sup>32</sup> See, e.g., *Rambus*, 2006 FTC LEXIS 60 at \*58 n.125 (citing, *inter alia*, *FTC v. Cement Inst.*, 333 U.S. 683, 694-95 (1948)).

<sup>33</sup> 15 U.S.C. § 2. The Commission's authority under Section 5 of the FTC Act reaches conduct that violates the Sherman Act.

<sup>34</sup> *Verizon Communs. v. Law Offices of Curtis v. Trinko*, LLP, 540 U.S. 398, 407 (2004).

<sup>35</sup> *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

<sup>36</sup> *Spectrum Sports v. McQuillan*, 506 U.S. 447, 456 (1993).

<sup>37</sup> 15 U.S.C. § 45(a), (n).

(a) **Rembrandt’s Clear Bad Faith Repudiation and Breach of the RAND Commitment Constitutes Exclusionary Conduct Under Section 2.**

The analysis of the exclusionary conduct at issue consists of two parts. First, we briefly show how Rembrandt’s license ‘offers’ and its multi-front litigation against some 14 parties – end-user networks, cable companies and manufacturers – constitute a clear repudiation and breach of the RAND commitment. Second, we explain how Rembrandt’s repudiation and/or breach of the RAND commitment – despite the apparent absence of any deceptive inducement by AT&T itself with respect to its RAND commitment – meets the standard for bad faith conduct *qua* exclusionary conduct, as highlighted in such cases as *Rambus*, *Unocal*<sup>38</sup> and *Qualcomm*.<sup>39</sup>

Taken as a whole, Rembrandt’s bad faith repudiation and breach had the effect of subverting the normal process of competition for the standard. By this conduct, Rembrandt exploited the monopoly which had been conferred first on AT&T (as predecessor) through the selection of technology for the ATSC standard that Rembrandt now claims infringes the ‘627 patent and then by adoption of the ATSC standard as a federally mandated standard.

(i) **Rembrandt has repudiated and breached the RAND commitment.**

Rembrandt has repudiated and breached the RAND commitment. The main points are as follows:

- ***Rembrandt has unequivocally repudiated the RAND commitment.*** In the litigation described above Rembrandt has claimed the ‘627 is essential to practicing the ATSC standard and then unequivocally denied any obligation to comply with the ATSC RAND commitment, stating as follows: “None of AT&T’s or AT&T IPM’s actions with regard to the ATSC standard or ATSC patent policy created a contractual right or other right, directly or as third party beneficiaries, between AT&T and Harris or Harris’ customers to license the ‘627 patent.”<sup>40</sup> Rembrandt took the same position in the breach of contract action filed by Harris in federal court in Florida – a position which now underlies its multidistrict litigation against end-users, networks, cable companies and manufacturers. These words and actions constitute a clear repudiation of the RAND requirement.

- ***Rembrandt’s position is inconsistent with the FCC policy.*** The FCC’s adoption of the ATSC standard as a federally mandated, exclusive standard for digital television was explicitly conditioned on “reasonable and nondiscriminatory licensing of relevant patents” by the ATSC members.<sup>41</sup> The FCC furthermore made it clear in earlier phases of the ATV proceeding, which began in 1987, “that, in order for DTV to be successfully implemented, the patents on the technology would have to be licensed *to other*

<sup>38</sup> *In the Matter of Union Oil Co. of Calif.*, No. 9305, 2005 FTC LEXIS 116 (F.T.C. July 27, 2005) (“*Unocal*”) (consent order) (resolving allegations under Section 5 that Unocal made deceptive and bad faith misrepresentations to a state standards-determining board concerning the status of Unocal’s patent rights; that the board relied on these misrepresentations in promulgating new standards for low-emissions gasoline; that Unocal’s misrepresentations led directly to its acquisition of monopoly power and harmed competition after refiners became locked in to regulations requiring the use of Unocal’s proprietary technology; and requiring, *inter alia*, that Unocal cease all efforts to enforce its relevant patents).

<sup>39</sup> *Broadcom Corp. v. Qualcomm, Inc.*, 501 F.3d 297 (3d Cir. 2007) (“*Qualcomm*”) (discussed below).

<sup>40</sup> See fn. 21, *supra*.

<sup>41</sup> Fourth Report and Order, ¶ 55.

*manufacturing companies* on reasonable and nondiscriminatory terms.”<sup>42</sup> The subsequent essentiality claim and failure by Rembrandt, as assignee, to make a bona fide RAND licensing offer therefore violates the RAND commitment.

- ***Rembrandt’s licensing demands are inconsistent with industry practice.*** Based on *Georgia-Pacific*, courts routinely look to evidence of custom and practice in the field to interpret RAND licenses.<sup>43</sup> Here, the custom and practice shows that patent-holder ATSC members license on a RAND basis. Moreover, unlike Rembrandt’s attempts to “double dip,” other licensors do not seek royalties from both manufacturers and end-users. In this regard, then, Rembrandt’s failure to make a bona fide RAND license offer to any manufacturer, and its demand to end-users, upsets the reasonable expectations of all potential manufacturer-licensees and other interested entities based on the custom and practice of other patent holders under the ATSC standard.

- ***Rembrandt’s proposed royalty amounts are clearly unreasonable and thus violate the RAND commitment.*** Rembrandt’s royalty demand to the broadcast networks amounts to almost ten times the entire sales price of ATSC-compliant transmitters sold by the manufacturers to the broadcast networks. It should be noted that this ‘ten times’ multiple is not ten times a reasonable royalty rate, but instead ten times a *100 percent* royalty rate.<sup>44</sup> With such a disparity between what Rembrandt is seeking from the end-user networks and what similarly situated patent holders charge the manufacturers, or between Rembrandt’s royalty demand and the manufacturers’ revenue from relevant sales, breach of the RAND commitment is indisputable.

(ii) **Rembrandt’s clear repudiation and breach of the RAND commitment constitutes exclusionary conduct.**

To be “exclusionary,” suspect conduct must be anticompetitive, in the sense of harming the competitive process and not merely harming competitors.<sup>45</sup> As Areeda and Hovenkamp put it, “‘exclusionary’ behavior should be taken to mean conduct other than competition on the merits – or other than restraints reasonably ‘necessary’ to competition on the merits – that reasonably appears capable of making a significant contribution to creating or maintaining monopoly power.”<sup>46</sup> And, under the still-generally accepted test, conduct is not deemed to be anticompetitive on balance unless the plaintiff shows that the anticompetitive harm from the conduct outweighs any countervailing procompetitive benefits.<sup>47</sup>

<sup>42</sup> *Id.* at ¶ 54 (emphasis added).

<sup>43</sup> *Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970) (citing, as one of the evidentiary factors to consider in determining a reasonable royalty for a patent license, the “portion of the profit or of the selling price that may be customary in the particular business or comparable businesses to allow for the use of the invention or analogous inventions”).

<sup>44</sup> See, e.g., *Georgia-Pacific*, 318 F. Supp. at 1120, *supra*, regarding evidentiary factors, including custom and practice, for determining a reasonable royalty.

<sup>45</sup> See, e.g., *United States v. Dentsply International*, 399 F.3d 181 (3d Cir. 2002), *cert. denied*, 126 S.Ct. 1023 (2006).

<sup>46</sup> Areeda and Hovenkamp, *Antitrust Law*, ¶ 651f (2006). Furthermore, “‘exclusionary’” comprehends at most behavior that not only (1) tends to impact the opportunities of rival but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way.” *Id.* at § 651b.

<sup>47</sup> *United States v. Microsoft*, 253 F.3d 34, 59 (D.C. Cir. 2001) (“the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit”); *Rambus*, 2006 FTC LEXIS 60 at \*67 (accepting balancing test and rejecting “profit sacrifice” test – which finds conduct exclusionary only if it would not have been profitable to the defendant but for the expectation that the conduct would exclude rivals or permit the defendant to

**Competition for the standard.** In the context of standard setting, as discussed above, the relevant competitive process is the competition for the standard, *ex ante*, which takes place among members of the standard setting organization. The success of cooperative standard setting vitally depends on SSO participants' obtaining information needed to select the optimal technology for the standard, based on an evaluation of costs as well as benefits. A commitment to license on RAND terms provides important information about future costs of licensing the standardized technology. Such information enables and enhances competition for the standard. Thus, a firm's RAND commitment – no less than its adherence to disclosure obligations, as in *Rambus* – is an important consideration for an SSO in evaluating the suitability of a given proprietary technology vis-à-vis competing technologies. As the Third Circuit noted in *Qualcomm*, which concerns an allegedly false RAND commitment, “[t]he FRAND commitment, or lack thereof, is . . . a key indicator of the cost of implementing a potential technology.”<sup>48</sup>

**Distortion of competition for the standard.** The contest for the standard is procompetitive when participants are informed about the relative technical merits and relative costs – but it can be anticompetitive if used for exclusionary purposes, through conduct that distorts the process. Here, the ATSC members, in choosing a technology to include in the standard, not only evaluated the technical merits of the mandated technology vis-à-vis alternative technologies but also took into account the likely cost of licensing it in order to manufacture goods based on the standard. And, as set forth in the Facts, there was competition for the RF transmission modulation technology.

As discussed above, standard setting is a cooperative process and requires good faith compliance with disclosure and RAND licensing rules. The cooperative character of standard setting creates particular opportunities for distortion of the process of competition for the standard.<sup>49</sup> As the court in *Qualcomm* explained, with particular relevance here, “[m]isrepresentations concerning the cost of implementing a given technology may confer an unfair advantage and bias the competitive process in favor of that technology's inclusion in the standard.”<sup>50</sup> Among other government and private actions, both the FTC, in *Rambus*, and the Third Circuit, in *Qualcomm*, have identified deception or misrepresentation as

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recoup its losses – as unsuitable for conduct that reduces consumer welfare but is inexpensive to execute (i.e., “cheap exclusion”).

<sup>48</sup> 501 F.3d at 313 (3<sup>rd</sup> Cir. 2007) (citing *F.T.C. v. Indiana Fed'n of Dentists*, 476 U.S. 447, 461-62 (1986) (noting that effort to obscure “information desired by consumers for the purpose of determining whether a particular purchase is cost justified is likely enough to disrupt the proper functioning of the price-setting mechanism of the market that it may be condemned” under antitrust law.). See also *Rambus*, 2006 FTC LEXIS 60 at \*5 (noting that FRAND commitments “may further inform [SSO] members' analysis of the costs and benefits of standardizing patented technologies”).

<sup>49</sup> See, e.g., *Rambus*, 2006 FTC LEXIS 60 at \*71 (explaining, with reference to the government's suit against Microsoft, how the finding of exclusionary conduct was based in part on deception by the company in a cooperative context: “In light of the expectations of a cooperative relationship, Microsoft's deceptive conduct was opaque. Consequently, countermeasures were hard, if not impossible, to implement and there was a substantial threat of competitive harm. [. . .] In contrast, deceptive conduct in competitive environments is less likely to be actionable under Section 2, because misrepresentations, deceptive practices, or omissions in the context of competitive relationships are less likely to be material.”).

<sup>50</sup> *Qualcomm*, 501 F.3d at 313 (citing *Allied Tube*, 486 U.S. at 501 (noting the need for private standard setting to be free “from being biased by members with economic interests in stifling product competition”)); see also *Broadcom v. Qualcomm*, 2007 WL 2296441 at \*15 (D.N.J. Aug. 31, 2006) (district court decision, acknowledging that intentional concealment of IPRs deprived SSO of opportunity to design around patented technologies in developing standard; district court's dismissal on grounds that this conduct nonetheless did not harm competition was reversed on appeal). In each of these cases, the harm lies in a party's obscuring cost and pricing information that is critical to the SSO members' choice of the standard from alternative, competing technologies. Such distortion can lead to anticompetitive results.



exclusionary conduct that satisfies the required showing of willful acquisition or maintenance of monopoly power under Section 2. The decisions in both *Rambus* and *Qualcomm* held that deception can constitute exclusionary conduct because “distorting choices through deception obscures the relative merits of alternatives and prevents the efficient selection of preferred technologies.”<sup>51</sup> Furthermore, where, as a result of such conduct, patent-related information comes to light only after the SSO has “complete[d] its lengthy process of evaluating technologies and adopting a new standard” and industry participants are locked-in to the new standard, the patent holder gains the power to collect supracompetitive royalties and consumer welfare suffers.”<sup>52</sup>

***Bad faith with respect to the RAND commitment.*** Bad faith in repudiating and breaching a RAND commitment, no less than the deceptive inducement alleged in such cases as *Rambus* and *Qualcomm*, is opportunistic, exclusionary conduct that can undermine standard setting. A RAND commitment induces reliance – it creates an expectation on the part of the other SSO participants. Reliance is thus triggered not only by the act of giving the commitment itself (without which the patent holder’s technology typically would not be permitted to be included in the standard), but by the expectation that the commitment will be fulfilled – that a license on RAND terms will be granted when the owner of the technology claims it is essential – in accordance with the principle of good faith and fair dealing. When that commitment is false or subsequently repudiated and breached, the other SSO members’ reasonable expectation that the commitment will be fulfilled is undercut, and the standard setting process is undermined. So here, the RAND commitment – the promise to do an act in the future – provided important information for determining the technology to be included in the standard, as part of the competition for the ATSC standard; it induced reliance; and it materially contributed to persuading the ATSC members to select the RF transmission modulation technology, which Rembrandt now asserts is essential to the standard and the implementation of which, it asserts, infringes the ‘627 patent. The commitment was not fulfilled, however, so the basis upon which the technology was included in the standard – again, the process of competition for the standard – was distorted.

Whether there was any deception or bad faith in inducing the SSO members to choose the technology for the standard should not affect the analysis. Any ultimately false commitment that upsets the reasonable expectations of the SSO members will have the

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<sup>51</sup> *Rambus*, 2006 FTC LEXIS 60 at \*62 (citing *FTC v. Ind. Fed’n of Dentists*, 476 U.S. 447, 461-62 (1986) (describing the anticompetitive consequences of “an effort to withhold (or make more costly) information desired by consumers for the purpose of determining whether a particular purchase is justified”)); *Qualcomm*, 501 F.3d at 313. *Rambus*, of course, concerns an allegation (and finding by the FTC) of deception in the failure to disclose intellectual property relevant to the standard, in violation of JEDEC’s disclosure rules, policy and an obligation of good faith and fair dealing. Similarly, in oral argument before the Third Circuit in *Qualcomm*, in which Broadcom charged Qualcomm with violating Sect. 2, among other claims, by breaching its FRAND commitment to an SSO on wireless telephony, the Court queried Broadcom counsel regarding the scienter requirement for monopolization, focusing on the defendant’s alleged misrepresentation with respect to its FRAND commitment. Counsel for Broadcom responded that Qualcomm “never intended to abide by [the FRAND obligation]” and, further, that Qualcomm had stated in its briefs below and on appeal that it “had no obligation to abide by it . . . [and that it has] no obligation to license at all under this FRAND commitment.” *Broadcom v. Qualcomm*, Case No. 06-4292, Transcript of Oral Argument before the Third Circuit Court of Appeals, June 28, 2007, at pp. 5-6 (remarks by George Cary, counsel for Broadcom). The Third Circuit, in reversing the district court’s grant of the motion to dismiss, held on the allegations before it that “(1) in a consensus-oriented private standard-setting environment, (2) a patent holder’s *intentionally false promise* to license essential proprietary technology on FRAND terms, (3) coupled with an SDO’s reliance on that promise when including the technology in a standard, and (4) the patent holder’s subsequent breach of that promise, is actionable anticompetitive conduct.” *Qualcomm*, 501 F.3d at 313.

<sup>52</sup> *Qualcomm*, 501 F.3d at 310.

same effect as deception or bad faith in the inducement.<sup>53</sup> Had the other ATSC members known that the technology they selected could lead to patent holdup, they doubtless would have chosen an alternative technology.

Several authoritative commentators have explained that a bad faith repudiation or breach of a RAND commitment can violate the antitrust laws, even absent evidence of deceptive inducement. As Professor Farrell and his co-authors explain in a recent article, “*demanding non-FRAND royalties ex post is either deceptive (the patent holder’s representation that it would offer FRAND licenses was untruthful) or the breaking of a commitment (the patent holder subsequently decided not to honor its FRAND commitment).*”<sup>54</sup> They further explain that RAND hold-up cases concern the “interpretation and enforcement” of the conditions (such as the RAND commitment) imposed on the approval of a patent holder’s increase in market power through selection of its intellectual property for the standard. But the focus of these cases on the interpretation and enforcement of the rules (such as RAND), as predicates for approval of a standard incorporating a participant’s intellectual property, does not mean the analysis should be restricted to cases of deceptive inducement: “[a]lthough these cases share elements with garden variety breach of contract disputes, they typically raise antitrust issues as well, since a failure by the patent holder to license on FRAND terms imposes costs on final consumers, not just on direct licensees.”<sup>55</sup> And as these commentators conclude, antitrust enforcement may be appropriate where “a patent owner may make FRAND or other similar commitments, then transfer relevant patents to another company that then claims not to be bound by those commitments”<sup>56</sup> – precisely the scenario presented in this matter.

***Rambus’s bad faith conduct satisfies the standard for “exclusionary conduct” in standard setting established in Allied Tube and relied upon in Rambus.*** The Supreme Court’s *Allied Tube* decision<sup>57</sup> and the FTC’s *Rambus* and *Unocal* actions clearly establish that exclusionary conduct in standard setting cases is not limited to deceptive conduct, but rather can include a broad range of opportunistic conduct. One of the key lessons from *Allied Tube* is that the predicate exclusionary conduct in standard setting is not limited to deception – and may even literally comport with an SSO’s rules – because opportunistic conduct that subverts the standard-setting process and harms competition can take various forms. As FTC Complaint Counsel said in a pre-trial brief in *Rambus*, “[t]here is no prescribed form of conduct that must exist before antitrust law can take effect as a mechanism for ensuring that the public interest is served through an industry standard-setting process. Theoretically, *any form of conduct – deception or otherwise* – that subverts the

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<sup>53</sup> Whatever the analytical or factual shortcoming that may have prevented the Commission from finding an antitrust violation in *N-Data*, such as an insufficient showing of causation, we submit that there are no such shortcomings here.

<sup>54</sup> J. Farrell, J. Hayes, C. Shapiro and T. Sullivan, “Standard Setting, Patents, and Hold-Up,” 74 Antitrust L.J. 603, 659 (Issue 3, 2007) (emphasis added).

<sup>55</sup> *Id.*

<sup>56</sup> *Id.*

<sup>57</sup> *Allied Tube and Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492 (1988). The Commission relied extensively on *Allied Tube* in its *Rambus* decision. See, e.g., *Rambus*, 2006 FTC LEXIS 60 at \*229 (citing *Allied Tube*, 486 U.S. at 500-01, 510, and stating that “[c]ourts and commentators long have recognized that a fair, honest, and consensus-based standard-setting process can be beneficial to consumers, while substantial competitive concerns may arise when the standard-setting choices of the SSO’s participants are distorted.”). See also, Herbert Hovenkamp et al., *IP and Antitrust*, v. II, at § 35.5 (2008 Supp.) (discussing *Allied Tube* as paradigm case of manipulation of standard setting).

proper ends of a standard-setting collaboration, causing the process to be corrupted, and the public interest to be harmed, could give rise to antitrust concerns.”<sup>58</sup>

In *Allied Tube*, the Court of Appeals found that although Allied acted within the letter of the rules, its conduct nonetheless “circumvented” the rules of the SSO (the National Fire Protection Association – NFPA), “subverted” the NFPA’s process, “violated the integrity” and was “inconsistent with the intent” of the NFPA’s procedures, was “inconsistent with the concept of ‘consensus’ standard-making,” and was done with the purpose “of achieving an anticompetitive result – the exclusion of PVC conduit from the marketplace.”<sup>59</sup> But, in an often repeated refrain, the Court of Appeals “refused to permit a defendant to use its literal compliance with a standard-setting organization’s rules as a shield to protect such conduct from liability.”<sup>60</sup> In the absence of a duty imposed by the SSO’s rules themselves, then, the Court of Appeals nonetheless identified a duty of good faith as the basis of liability. Similarly, in *Rambus*, Complaint Counsel contended that Rambus’s conduct “violated the general requirement of good faith.”<sup>61</sup> And so also, here, Rembrandt’s repudiation and breach of the RAND commitment violates the duty of good faith articulated in and underpinning *Allied Tube* and relied upon in *Rambus*. Rembrandt’s conduct is exclusionary and satisfies precedent established by *Allied Tube* and *Rambus*, among other cases, because it “subverted” the ATSC’s process and goals, was “inconsistent with consensus standard-making” and was carried out with the purpose “of achieving an anticompetitive result.”<sup>62</sup>

In short, when the choices made to select technologies for the ATSC standard are predicated on false representations, whether through deception in the inducement *or* a subsequent bad faith failure to execute on the promise, then monopoly power has been achieved not on the merits of competition for the standard but instead through subversion of the standard setting process itself. In these circumstances, when a promise to do a future act is later repudiated or breached, whether by the original promisor itself or by a subsequent assignee, and that repudiation or breach cannot be excused by accident or other legally justified cause, but instead results from bad faith, it is immaterial whether the intent not to honor the commitment is formed only after it is originally made. The key is whether the conduct in question clearly upsets or would have upset the reasonable expectations of the SSO members in their selection of a standard. The anticompetitive consequences are no different from those in the more conventional scenario of a contemporaneous intent to deceive at the time of making the commitment (as in *Rambus* and allegedly in *Qualcomm*): the relative merits and efficient selection of alternative technologies are distorted.<sup>63</sup>

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<sup>58</sup> *Rambus*, Complaint Counsel’s Memorandum in Opposition to Respondent Rambus Inc.’s Motion for Summary Decision, at 41 (March 25, 2003) (emphasis added).

<sup>59</sup> *Allied Tube*, 817 F.2d at 947.

<sup>60</sup> *Id.*

<sup>61</sup> Complaint Counsel’s Memorandum in Opposition to Rambus Motion for Summary Decision, at 24 (March 25, 2003) (contending further that “[by] depriving JEDEC of critical important, patent-related information, Rambus manipulated an otherwise pro-competitive, open standards process, causing that process to become a vehicle for endowing monopoly power upon a single firm, to the enduring detriment of JEDEC and its broader membership, not to mention the relevant markets at issue in this case.” *Id.*). See also *Rambus*, Complaint at ¶ 54 (June 18, 2002) (alleging deception and bad faith conduct), and Appeal Brief of Counsel Supporting the Complaint, at 28, 48-53 (April 16, 2004) (alleging that Rambus’s course of conduct breached Rambus’s duty of good faith and violated its specific obligations under JEDEC rules and customs).

<sup>62</sup> See *Allied Tube*, 817 F.2d at 947.

<sup>63</sup> See *Rambus*, 2006 FTC LEXIS 60 at \*62; *Qualcomm*, 501 F.3d at 313.

As Professors Hovenkamp, Janis and Lemley explain in their treatise, “the competitive risk [in the consensus process that characterizes standard setting] is that the misrepresentation will cause a standard-setting organization to adopt a standard it otherwise would have rejected, and it would not otherwise have obtained.”<sup>64</sup> Thus, what matters is the outcome – the distortion of competition for the standard through the obscuring of cost and pricing information that SSO participants needed to make an informed selection of a standard from competing, alternative technologies – and the fact that the SSO relied on a commitment that was ultimately breached and repudiated.

***Special concerns of the conduct of NPEs.*** Finally, as a general matter, a narrow test for exclusionary conduct in this context would promote intellectual property transfers that would undermine the standard setting process and harm consumers. Intellectual property transfers can be used as a ruse to avoid the obligations of a standard setting process. NPEs in particular can significantly undermine standard setting by acquiring intellectual property rights at a premium with the goal of enhancing licensing revenues by repudiating RAND obligations. A legal test requiring deception or bad faith at the time a RAND commitment is given would countenance such exclusionary and competitively harmful conduct. Thus, the test of exclusionary conduct must be interpreted with sufficient flexibility – or, more precisely, in reliance on the core principle of good faith and fair dealing as articulated in *Allied Tube* – to capture repudiation or breach of a RAND commitment.

Given NPEs’ business incentives, such conduct may become more widespread unless the opportunity is taken on the appropriate set of facts, such as here, to establish that such conduct can be “exclusionary” under Section 2. NPEs pose a far more significant threat of patent holdup and other types of opportunistic conduct. The business model of NPEs is vastly different than that of the typical participants in standard setting – technology development companies and manufacturers. NPEs do not need to cooperate with other holders of intellectual property and do not need to license intellectual property. The fear of reprisal from fellow technology or manufacturing companies, which may animate the good faith conduct of many SSO participants, does not inhibit NPEs. The increasing opportunities for NPEs to engage in patent hold-up, as NPEs continue to expand their role in patent licensing today, and the absence of the usual constraints on such conduct, therefore suggest the need for heightened scrutiny of NPEs, to ensure that they adhere to standard setting rules, such as RAND commitments.<sup>65</sup>

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<sup>64</sup> Herbert Hovenkamp et al., *IP and Antitrust*, v. II, § 35.5(6) at 35-48 (2008 Supp.).

<sup>65</sup> See William Blumenthal (General Counsel, FTC), “Some Discussion Questions on Standard Setting and Technology Pools,” ABA Antitrust Section Fall Forum (Nov. 15, 2007) (questioning whether there should be heightened scrutiny when the successor owner of technology included in a standard is an NPE, and citing as possible reasons for heightened scrutiny the fact that (i) NPEs frequently do not participate in SSOs and so are not concerned about their reputations within SSOs and (ii) NPEs do not need to obtain patent licenses from others and so are not subject to retaliation for bad conduct. See also *N-Data*, Statement of the Commission (Jan. 23, 2008) (regarding allegations of patent hold-up in proposed consent agreement with NPE N-Data, majority Statement that “if N-Data’s conduct became the accepted way of doing business, even the most diligent standard-setting organizations would not be able to rely on the good faith assurances of respected companies. The possibility exists that those companies would exit the business, and that their patent portfolios would make their way to others who are less interested in honoring commitments than in exploiting industry locking.”). And see generally Fed. Trade Comm’n, To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy ch. 2 at 31, n.220; ch. 3 at 38-41, available at <http://www.ftc.gov/os/2003/10/innovationrpt.pdf> (2003) (conduct by NPEs, sometimes referred to as ‘patent trolls’, may harm consumers when such firms force manufacturers to agree to licenses after the manufacturers have sunk substantial investments into technologies).

(b) **Rembrandt Willfully Acquired and Maintained Monopoly Power By Repudiating and Breaching the RAND Commitment.**

The selection of patented technology for inclusion in a standard clearly augments the potential power of the owner of the selected technology. Here, there has been no determination that practicing the ATSC standard infringes the '627 and, as noted above, the defendants in the respective intellectual property actions take the position that their products do not infringe the '627. Nevertheless, the *assertions* by Rembrandt that the '627 technology is essential to the ATSC standard, and its multiple lawsuits based on those assertions, combined with the FCC's order mandating the ATSC standard as the sole commercial standard for DTV, have conferred on the owner of the '627 a monopoly in the technology market for DTV RF transmission modulation technology.

Monopoly here, however, must be distinguished from monopoly power. The prior owners of the '627, assuming they claimed the '627 to be essential to the standard, and until assignment to and repudiation by Rembrandt, had a monopoly in the relevant market because of the adoption of the standard; but they did not have monopoly *power*, because their power to exploit the monopoly through supracompetitive pricing, or even through declining to license the technology, was constrained by the RAND commitment.<sup>66</sup> When Rembrandt then rejected this constraint, it engaged in illegal monopolization. Once having been assigned the patent and acceded to the monopoly position corresponding to it because of the adoption of the standard, Rembrandt opportunistically exploited the monopoly when it repudiated and breached the RAND commitment. In this way, Rembrandt willfully acquired and exercised monopoly power in the relevant market in violation of Section 2.

The RAND commitment, to which Rembrandt is bound,<sup>67</sup> is thereby causally linked to the adoption of the ATSC standard by the FCC: the commitment materially contributed to the adoption of the standard.<sup>68</sup> Assuming AT&T asserted that the '627 was essential, then the federally mandated ATSC standard in turn would have conferred monopoly power on AT&T and its successors *but for* the RAND commitment and the accompanying obligation of good faith and fair dealing to satisfy its terms. It therefore follows that when a successor repudiates or breaches the RAND commitment, that successor achieves and exercises monopoly power precisely through its repudiation and breach. Thus, Rembrandt acquired monopoly power as a result of its exclusionary conduct – the repudiation and breach. Antitrust causation is thereby established between the exclusionary conduct and the acquisition of monopoly power.<sup>69</sup>

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<sup>66</sup> In this sense, it may be said that the prior owners of the '627, in giving and/or abiding by the RAND commitment, 'negotiated away' the monopoly power they otherwise would have derived from the asserted inclusion of their intellectual property in the standard.

<sup>67</sup> The RAND commitment follows the patent. See fn. 42, supra. Accordingly, Rembrandt must be viewed legally as stepping into the shoes of AT&T, as if Rembrandt had made the commitment itself.

<sup>68</sup> Rembrandt was able to accede to a monopoly position as a result of a commitment that the ATSC members expected to be fulfilled: but for AT&T's commitment and the reasonable expectation that it would be fulfilled, the ATSC members would not even have considered the technology that Rembrandt now asserts is essential to the standard for inclusion in that standard.

<sup>69</sup> To the extent any small gaps may be found in this chain of causation, although we submit that there are none, it should be noted that exclusionary conduct need not be the exclusive cause of a monopoly position found to result from monopolization. Areeda and Hovenkamp explain why in these circumstances Section 2 monopolization should nonetheless apply: "because monopoly will almost certainly be grounded in part on factors other than a particular exclusionary act, no government seriously concerned about the evil of monopoly would condition its intervention solely on a clear and genuine chain of causation from an exclusionary act to the presence of monopoly. And so it is sometimes said that doubts should be resolved against the person whose behavior created the problem." Areeda and Hovenkamp,

## 2. Attempted Monopolization.

Even assuming a Section 2 monopolization claim were not found to be warranted on these facts, on the theory that Rembrandt has not yet received non-RAND royalties, the facts would support a claim of attempted monopolization. Rembrandt has engaged in exclusionary conduct, it has a specific intent to monopolize and there is a dangerous probability that it would achieve monopoly power through its conduct.<sup>70</sup>

First, the same kind of anticompetitive conduct that supports a monopolization case also supports an attempt case.<sup>71</sup> Second, the specific intent element can be satisfied with proof that the defendant had a specific intent to acquire monopoly power; it can be proven either by direct evidence or by inference from evidence of anticompetitive conduct. Here, the supracompetitive royalty demands, in violation of the RAND requirement, evidences the necessary specific intent. Finally, Rembrandt, by virtue of its assertions that anyone complying with the ATSC standard infringes the '627 patent, and the ensuing abusive enforcement efforts, create a dangerous probability of achieving monopoly power because all potential licensees are already locked in to the technology and there are no possible alternatives, particularly in light of the FCC mandate.

Any arguments that there has been no competitive harm because Rembrandt has not yet obtained satisfaction on its non-RAND demands are unavailing. In *Rambus*, for instance, Rambus argued that its conduct, even assuming it was deceptive, had no anticompetitive effect because its royalty rates were reasonable. The FTC rejected this argument, reasoning that even assuming, *arguendo*, that the rates were reasonable (and it found that they were not), “[d]eceptive conduct that confers durable market power by its very essence harms competition, and claims that the offender has not yet behaved like a monopolist provides no shelter.”<sup>72</sup> Thus, as the Court of Appeals said in *United States v. Microsoft*, “[i]f monopoly power has been acquired or maintained through improper means, the fact that the power has not been used to extract [a monopoly price] provides no succor to the monopolist.”<sup>73</sup> This principle further supports the contention that although Rembrandt has not yet received satisfaction on its royalty demands, it has at a minimum created a dangerous probability of success and so has engaged in attempted monopolization – if not monopolization itself – under Section 2.

## 3. Section 5 of the FTC Act: Unfair Method of Competition and Unfair Act or Practice

Even if the FTC were to conclude that Rembrandt’s conduct does not rise to the level of a Sherman Act violation, it nonetheless would constitute a violation of Section 5 of

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*Antitrust Law*, ¶ 651b (2006). See also *Rambus*, 2006 FTC LEXIS 60 at 189-91 (rejecting Rambus’s argument for imposing “but for” causation burden on Complaint Counsel – i.e., to show that Rambus’s conduct was the sole cause of Rambus’s monopoly position – and noting that “[i]n an equitable enforcement action, it is sufficient that the exclusionary conduct reasonably appears capable of making a significant contribution to creating or maintaining monopoly power” (citations omitted)).

<sup>70</sup> See *Spectrum Sports v. McQuillan*, 506 U.S. 447, 456 (1993) (setting forth elements).

<sup>71</sup> See, e.g., *Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377 1382 (9<sup>th</sup> Cir. 1983).

<sup>72</sup> *Rambus*, 2006 FTC LEXIS 60 at \*275.

<sup>73</sup> 253 F.3d 34, 56-58 (D.C. Cir.), *cert. denied*, 534 U.S. 952 (2001), quoting *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 274 (2d Cir. 1979), 444 U.S. 1093 (1980).

the FTC Act, which prohibits “unfair methods of competition” and “unfair acts or practices.”<sup>74</sup>

The FTC’s recent proposed complaint and consent order with licensing company N-Data for alleged patent hold-up offers a useful guide for application of Section 5 to this type of patent holdup.<sup>75</sup> The proposed consent order in *N-Data* is based on allegations that N-Data repudiated certain licensing commitments that its predecessor gave to a standard setting organization. The Commission found that N-Data violated Section 5 by renegeing on a 1994 letter commitment by National Semiconductor Corporation to the IEEE to license on specified terms certain patented technology relating to Ethernet. National had assigned the relevant patents to Vertical Networks, which in turn assigned them to N-Data in November 2003. For substantially the same reasons that the Commission found that N-Data’s conduct constituted an “unfair method of competition” and an “unfair act or practice” under Section 5 in *N-Data*, Rembrandt’s conduct here would also violate these provisions of Section 5.

First, Rembrandt’s conduct – bad faith behavior that distorts competition for the standard and so undermines the standard setting process and raises prices – constitutes an unfair method of competition even if it were found for some reason not to infringe either the letter or spirit of the antitrust laws.<sup>76</sup> The conduct also satisfies the commonly accepted limiting principles for application of the ‘unfair method of competition’ prong of Section 5: the patent hold-up is “coercive” and “oppressive” with respect to firms locked into the standard<sup>77</sup> and the conduct is having or threatens to have an adverse impact on competition.<sup>78</sup>

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<sup>74</sup> Section 5 prohibits “unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce.” 15 U.S.C. § 45(a)(1).

<sup>75</sup> *N-Data*, FTC File No. 051-0094, Agreement Containing Consent Order (Nov. 9, 2007), Statement of the Commission (Jan. 23, 2008), and Proposed Complaint.

<sup>76</sup> See, e.g., *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233 (1972); see also *N-Data* (Analysis to Proposed Consent Order to Aid Public Comment).

<sup>77</sup> See, e.g., *Official Airline Guides v. FTC*, 630 F.2d 920 (2d Cir. 1980) (“OAG”) (spelling out coercion requirement), and *E.I. Du Pont v. de Nemours & Co. v. FTC*, 729 F.2d 128, 139-40 (2d Cir. 1984) (“Ethyl”) (“oppressiveness”).

<sup>78</sup> See *N-Data* (Analysis of Proposed Consent Order to Aid Public Comment). It should be noted that if Rembrandt were demanding royalties from the manufacturers, even though on a non-RAND basis, at the same time that it is demanding royalties from the end-user broadcast networks and cable companies (as described herein), this conduct arguably would itself constitute unfair competition within the meaning of Section 5. Recovery of royalties from two (vertically situated) licensees of patent rights for the same use of those rights has been held to constitute an impermissible extension of patent rights, triggering the affirmative defense of patent misuse to an infringement claim and rendering the patent unenforceable. See, e.g., *PSC, Inc. v. Symbol Technologies, Inc.*, 26 F. Supp.2d 505, 510 (W.D.N.Y. 1998) (holding that Symbol Tech.’s rights under the patents at issue were extinguished and that Symbol forfeited its right to collect any additional royalties on any product that practiced any claim under the relevant patents and that used a device manufactured by PSC based on those same patents); see also *Cyrix Corp. v. Intel Corp.*, 846 F. Supp. 522, 539 (E.D. Tex.) (noting that the purpose of the exhaustion doctrine is to “prevent [ . . . ] patentees from extracting double recoveries for an invention . . .”), *aff’d*, 42 F.3d 1411 (Fed. Cir. 1994). (It should also be noted that the exhaustion doctrine, also known as the “first sale doctrine,” and the exception to that doctrine, the conditional sale doctrine, are under review by the Supreme Court in *Quanta Computer, Inc. v. LG Electronics*, No. 06-937, although the precise issue before the Court in that case is permissible conditioning of subsequent use or resale following an authorized sale.)

Here, Rembrandt’s efforts to secure royalties from the manufacturers for their alleged use of the ‘627 in manufacturing ATSC-compliant transmitters and also from the networks for their use of the transmitters in television broadcasting (and as a percentage of their revenues) would constitute patent misuse (and also possibly an independent ground for a violation of Section 2, if the requisite effects on competition are shown). The theory is that the patentee’s rights are extinguished, under the doctrine of patent exhaustion, once the patentee has obtained royalties from the manufacturer, who allegedly uses the patent in making a product. Here, as explained above, Rembrandt is required to offer a license, on RAND terms, to the manufacturers; thus, any demand for royalties simultaneously from the manufacturers’ customers arguably triggers the exhaustion doctrine. Furthermore, even if there is no patent misuse until

Second, Rembrandt's conduct constitutes an unfair act or practice under Section 5(n).<sup>79</sup> As interpreted by the Eleventh Circuit in *Orkin Exterminating Co. v. FTC*,<sup>80</sup> Section 5(n) requires a showing that (1) the conduct caused "substantial consumer injury," (2) the injury is "not . . . outweighed by any countervailing benefits to consumers or competition that the practice produces" and (3) it is an injury that "consumers themselves could not reasonably have avoided." Just as the Commission found that N-Data's conduct satisfied these criteria, so here, Rembrandt's conduct also would support a finding of a Section 5 violation on the 'unfair act or practice' prong: Rembrandt opportunistically exploited the RAND commitment on which the ATSC members relied in selecting the ATSC standard; the industry has become locked in to the technology which Rembrandt now asserts is essential to the standard and for which it is now demanding exorbitant royalties; this conduct threatens to cause substantial consumer injury in the form of higher prices for the relevant equipment (set forth in more detail below); the conduct produces no articulable benefits to consumers or competition; and neither the ATSC members who reasonably expected the RAND commitment to be honored by AT&T IPM and its assignees, nor the end-user networks and cable companies, nor television viewers could reasonably avoid the injury they face as a result of Rembrandt's conduct.

#### IV. HARM TO COMPETITION

Rembrandt's conduct threatens severe harm to competition and harm to the ultimate consumers – television viewers. Rembrandt's conduct threatens to increase the price and reduce the output of products and services that implement the ATSC standard for use in digital television, thus raising prices and reducing output of digital television to the consuming public. In particular, the threatened harm includes the following:

- Rembrandt's conduct is subjecting digital equipment manufacturers to the threat of having to pay royalties that would far exceed the entire cost of their equipment that implements the ATSC standard. Those increased costs will be passed on to the ultimate consumers in higher prices.
- End-users are also being threatened with having to pay exorbitant royalties based on their use of such equipment, where demands for royalties from end-users are inconsistent with the RAND commitment both in terms of the identity of prospective licensees (i.e., end-users rather than manufacturers) and in royalty amount. Those excessive royalties will be passed on to the ultimate consumer.
- Every time a network or cable company increases the amount of digital broadcasting territory or content utilizing ATSC equipment, it is increasing its financial exposure and risk, due to the threat from Rembrandt. Thus, the networks and cable companies may have an incentive to slow down or cease transition to DTV altogether,

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there has been an actual recovery of 'double royalties', any such simultaneous demands for royalties from the manufacturers and their customers can be considered unfair competition under Section 5.

<sup>79</sup> Section 5(n) states: "The Commission shall have no authority . . . to declare unlawful an act or practice on the grounds that such act or practice is unfair unless the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition." 15 U.S.C. § 45(n) (1992).

<sup>80</sup> 849 F.2d 1354, 1364 (11<sup>th</sup> Cir. 1988).



thereby unwittingly undermining the FCC mandate as a result of Rembrandt's opportunistic conduct.

- The effect of the non-RAND royalties will likely lead to increased costs to all television viewers, dramatically increasing the price they pay for viewing digital television. Those costs may also lead to increased costs for television advertisers.
- Rembrandt's conduct also threatens to delay the federally mandated transition date to digital television and so delay and deprive the industry and television viewers of this innovation.

More generally, Rembrandt's conduct resulted in a distortion of competition for the ATSC standard with respect to DTV RF transmission modulation technology, foreclosing the choice of alternative, competing proprietary or non-proprietary technology that would not have resulted in patent hold-up. As a result of this conduct, digital equipment manufacturers may have decreased incentives to produce products that implement the ATSC standard. Manufacturers and other members of the industry may have decreased incentives to participate in further ATSC or other relevant standard setting activities. Furthermore, there may be a decreased reliance on standards developed by SSOs both within and without the industry for advanced television technology and telecommunications generally, all having the effect of undermining standard setting and precluding its intended procompetitive effects.

## V. RELIEF

We request that the Commission commence an investigation of Rembrandt's conduct and seek an order pursuant to Section 5(b) of the FTC Act requiring that Rembrandt cease and desist from its illegal conduct. In particular, the Commission should prohibit Rembrandt from enforcing the '627 patent unless it has first offered to license the '627 on terms consistent with the RAND commitment.

A failure to enjoin Rembrandt's conduct could result in owners (or subsequent owners) of ATSC patents engaging in similar patent-hold-up conduct that could cripple the DTV industry. Private remedies through patchwork litigation in different fora are inadequate substitutes for FTC enforcement in this matter: First, "private litigation may not vindicate the same set of public interests that are addressed by the Sherman Act or Section 5 of the FTC Act."<sup>81</sup> Second, by the time any resolution of such private suits has been achieved – and even assuming Rembrandt's claims were ultimately defeated – the February 2009 date for the transition to digital television will have long since passed and the mere threat of the harm described above will itself have caused irreparable harm to competition and to consumers alike.

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<sup>81</sup> A.F. Abbott and T.A. Gebhard, "Standard-Setting Disclosure Policies: Evaluating Antitrust Concerns in Light of *Rambus*," 16 Antitrust ABA 29, 33 (Summer 2002) citing this point as one of the policy justifications for an administrative remedy in *Rambus*).