The American Antitrust Institute

June 14, 2011

Federal Trade Commission
Office of the Secretary
Room H-113 (Annex X)
600 Pennsylvania Avenue, N.W.
Washington, DC 20580

Re: **Patent Standards Workshop, Project No. P111204**

Ladies and Gentlemen:

The American Antitrust Institute ("AAI") welcomes this opportunity to provide comments on "the practical and legal issues arising from the incorporation of patented technologies in collaborative standards" with particular reference to "the risk of patent 'hold-up' and its effect on competition and consumers."[1] The AAI has on several occasions supported and encouraged the Commission's actions to address the hold-up problem in connection with standards development activities. Patent owners that manipulate standards development processes to obtain the ability to enforce their patents in exclusionary ways against locked-in implementers of final standards are responsible for serious injury to competition and to the consuming public in all of the ways the Commission has articulated throughout the past 15 years (since the *Dell* case).[2] As we discuss below, the standards-setting organizations ("SSOs") that allow their processes to be so misused should be expected to do more to avoid that injury. We applaud the Commission for holding next week's workshop because it suggests interest in both continuing and deepening the agency's efforts in this area generally.

The Commission's Notice invites comments on 27 questions within three subjects of agency concern: Disclosure of Patent Rights in an SSO; the RAND Licensing Commitment; and Ex Ante Disclosure and/or Negotiation of Licensing Terms. We offer below a range of comments on each of these subjects in ways that address legal or policy aspects of the listed questions.

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[1] Fed. Trade Comm'n, Request for Comments and Announcement of Workshop on Standard-Setting Issues, 76 Fed. Reg. 28036 (May 13, 2011).

[2] *In re: Dell Computer Corp.*, 121 F.T.C. 616 (1996).

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A. <u>Disclosure of Patent Rights in an SSO</u>

The Commission asks "[w]hy" SSOs "adopt policies that may lead to incomplete disclosure of relevant patents."[3] A main explanation, in our view, is the divergence of interests and associated business models among the SSO participants that influence the policies that are adopted. While some participants are genuinely committed to open-standards outcomes as platforms for their product development activities, other participants are more interested in maximizing profits from enforcement of patents covering technologies incorporated into standard specifications. In short, the latter participants benefit from the very hold-up power that effective disclosure policies would help to prevent.

Put another way, SSO policies often result in incomplete disclosures because they are ineffectual compromises between differently motivated groups of participants. The interest of consumers and the public at large in the minimization of anticompetitive hold-ups is not adequately represented in those deliberations. Perhaps, in this light, the time has come for the Commission to remind the SSO community of the implications for the current standards development environment of the Supreme Court's decision 29 years ago in *American Society of Mechanical Engineers v. Hydrolevel Corp.*[4] The Court there established an SSO's strict antitrust liability in circumstances where anticompetitive harm occurs as a result of the SSO's failure to implement procedures aimed at preventing abuse of its processes. The Commission is well positioned to update and develop the law in this area; it can advise SSOs of their antitrust obligation to implement "effective" disclosure policies in contrast, for example, to the "vague and ambiguous" JEDEC policy that Rambus so easily circumvented and that was a contributing factor in the unfortunate last chapter of the Commission's *Rambus* case.[5]

The Commission's Notice suggests that among the reasons for incomplete disclosures may be the SSO's "not requiring members to search their patent portfolios[.]"[6] The broader problem, however, is that many SSOs not only disclaim the "search" obligation but limit the disclosure requirement altogether to patents that are known to the particular company employee who represents the company in the SSO process. As a result, the SSO implicates itself in willful ignorance of relevant patent positions. There is a more responsible middle course between a full-scale search and the

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[3] 76 Fed. Reg. at 28037.

[4] 456 U.S. 556 (1982).

[5] *See Rambus, Inc. v. FTC*, 522 F.3d 456, 468-69 (D.C. Cir. 2008); *see generally* Robert A. Skitol & Kenneth M. Vorrasi, *Patent Holdup in Standards Development: Life After* Rambus v. FTC, ANTITRUST, Summer 2009, at 26-33.

[6] 76 Fed. Reg. at 28037.

now-prevalent nothing-at-all expectation: an obligation of "good-faith reasonable inquiry" as a core part of the disclosure requirement. The Commission can and should promote that course or some variation on it as part of SSOs' *Hydrolevel* obligation to implement procedures aimed at preventing abuse of their processes.

The Commission also asks what "principles" should apply "in judging whether a patent holder's conduct before an SSO is deceptive" and, in particular, what should be "the role of the SSO's patent disclosure policy in judging whether conduct is deceptive or unfair[.]"[7] AAI believes the principles should be those set forth at length in (a) the Commission's final decision in the *Rambus* case for purposes of applying Section 2 of the Sherman Act (notwithstanding the D.C. Circuit's fundamentally flawed grounds for reversing the decision),[8] and (b) then-Commissioner Leibowitz's concurring *Rambus* opinion for purposes of applying Section 5 of the FTC Act.[9] We would note one qualification, however: a finding of deception or unfairness, or of unlawful "exclusionary" conduct arising from hiding the existence of an essential patent or from otherwise subverting a standards development process by withholding material patent-related information, should not depend on whether the conduct at issue technically violated the SSO's disclosure policy. SSO participants engaging in such conduct should not benefit from an ineffectual policy that they in all likelihood participated in drafting to be ineffectual.

Finally, the Commission asks whether "non-disclosure or lack of information about relevant patent rights subvert[s] the competitive process of selecting technologies for standards or undermine[s] the integrity of standard-setting activities."[10] AAI believes the answer is a resounding and unqualified yes – again for all of the reasons the Commission itself articulated in its *Rambus* decision. Non-disclosure denies standard-setting participants the ability to make informed choices among patented and patent-free solutions for their specifications. That inability forecloses any semblance of ex ante competition on the merits among technology sponsors. It also enables a patent owner to hijack the whole open standards effort and convert it into a proprietary monopoly.

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[7] *Id.* at 28037.

[8] *See Rambus, Inc.*, No. 9302, 2006 FTC LEXIS 60 (F.T.C. Aug. 2, 2006) (Commission Opinion on Liability).

[9] *See Rambus, Inc.*, No. 9302, 2006 FTC LEXIS 102 (F.T.C. Aug 2, 2006) (Concurring Opinion of Commissioner J. Leibowitz).

[10] 76 Fed. Reg. at 28037.

B. RAND Licensing Commitment

The Commission asks whether "RAND licensing commitments without accompanying disclosure commitments provide adequate protection against patent hold-up."[11] AAI believes the answer is a clear and unqualified no. Given the lack of any definition for or even guideposts around the meaning of "reasonable" in particular, an ex ante RAND commitment does not effectively constrain a patent owner's ex post license demands. Indeed, cases like *Broadcom Corp. v. Qualcomm, Inc.*[12] illustrate how SSO policies prescribing RAND commitments provide false assurances that enable and facilitate the very hold-up conduct they purport to protect against. For this reason, AAI believes the Commission should encourage more SSOs to move in the direction of more meaningful ex ante commitments such as ex ante disclosure of license terms and associated ex ante negotiation processes discussed in the next section below.

The Commission asks whether a RAND commitment should "preclude a patent owner from seeking in patent litigation" a preliminary or permanent injunction or an International Trade Commission exclusion order "against practice of the standard."[13] AAI believes the answer is a clear and unqualified yes. A RAND commitment must, at a minimum, be construed as a promise to extend reasonable license terms in the event a license becomes necessary to practice the standard. SSO participants should be able to rely on that promise as an assurance that, while not foreclosing future litigation over patent infringement or patent validity or over what license terms are reasonable, participants will not be excluded from the market altogether by an injunction or other prohibition upon the sale of their standard-compliant products.

The public interest element of injunctive relief law as discussed in the Supreme Court's *eBay* decision[14] strongly supports that proposition, as does Chapter 8 of the Commission's March 2011 Report on "The Evolving IP Marketplace."[15] AAI respectfully suggests at least two FTC enforcement policy ramifications. First, it should be an unfair method of competition and an unfair and deceptive practice for a patent owner that makes an ex ante RAND commitment on which SSO participants rely in deciding to incorporate the owner's technology into a final standard to seek injunctive relief or an exclusion order precluding practice of the standard. Second, SSOs should be

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[11] *Id.*

[12] 501 F.3d 297 (3d Cir. 2007).

[13] 76 Fed. Reg. at 28037-38.

[14] *eBay Inc. v. Merc Exchange, LLC*, 547 U.S. 388 (2006).

[15] *See* FED. TRADE COMM'N, THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION 213-244 (2011), *available at* http://www.ftc.gov/os/2011/03/110307 patentreport.pdf.

admonished to amend their patent policies to require patent owners, as an express element of any RAND commitment, to commit to foregoing injunctive or other exclusion relief against practicing the standard in any ex post patent litigation. In short, clarification that this is a part of what a RAND commitment means should be part of an SSO's *Hydrolevel* obligation to implement measures reasonably designed to protect against anticompetitive abuse of its processes.

The Commission asks under what circumstances should a RAND commitment "bind later owners of the patent[,]" what steps "can or should SSOs take to ensure that a transferred patent remains subject to a prior RAND commitment[,]" and does "reneging on a RAND commitment subvert the competitive process of selecting technologies for standards or undermine the integrity of standard-setting activities?"[16] AAI believes these questions are of paramount importance to any serious effort to mitigate hold-up risks in connection with standards development processes generally. This is because of the rapidly accelerating rate at which patents are now changing hands, promoted in particular by non-practicing entities ("NPEs") whose sole, or at least primary, reason for buying up patents from prior owners is to profit from enforcement against unsuspecting existing users of the patented technology. The Commission's *N-Data* complaint, consent order and related statements of two years ago[17] reflect an awareness of how an assignee of a patent subject to a license commitment to an SSO can engage in anticompetitive hold-up conduct by refusing to honor the assignor's promise. We applaud the manner in which the Commission applied both the unfair methods of competition prong and the unfair acts prong of Section 5 to N-Data's conduct in that action.

AAI believes the Commission should now build upon the *N-Data* precedent to address more robustly the patent hold-up risk in connection with patent ownership changes. First, a RAND commitment, like any license obligation, should run with the patent so that any subsequent assignee of the patent is deemed to have constructive notice of it and to be legally bound by it. Actual notice is thus not required for an assignee to be deemed to have assumed the RAND obligation.[18] In addition, SSOs themselves can and

[16] 76 Fed. Reg. at 28038.

[17] Fed. Trade Comm'n, FTC Challenges Patent Holder's Refusal to Meet Commitment to License Patents Covering 'Ethernet' Standard Used in Virtually All Personal Computers in U.S. (Jan. 23, 2008), *available at* http://www.ftc.gov/opa/2008/01/ ethernet.shtm (announcing proposed complaint and decision and order). After comments were submitted, the Commission's complaint and decision and order became final in September 2008. *See* Negotiated Data Solutions LLC, No. C-4234, 2008 FTC LEXIS 119 (F.T.C. Sept. 22, 2008) (Complaint); Negotiated Data Solutions LLC, No. C-4234, 2008 FTC LEXIS 120 (F.T.C. Sept. 22, 2008) (Decision and Order).

[18] *See, e.g., In re Cybernetic Servs. Inc.*, 252 F.3d 1039 (9th Cir. 2001) (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

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should take further steps to discourage patent transfers that might be used to avoid RAND commitments. In particular, SSOs should require that all participating patent owners expressly undertake to inform any subsequent assignee of their commitments and to make those commitments contractually binding on successors and assignees. Again, this should be part of the SSO's *Hydrolevel* obligation to take reasonable measures to minimize hold-up risks. The failure of an SSO to impose such a requirement, however, should not diminish the liability of an assignee that engages in hold-up conduct through repudiation of a prior owner's commitment.

We note in that regard that the legal basis for the *N-Data* settlement was limited to the unfair methods of competition and unfair acts prongs of Section 5. In the majority statement, the Commission cited the absence of any deception on the part of N-Data itself, as an assignee of the original licensing obligation, as one reason for not also grounding the settlement in Section 2 of the Sherman Act.[19] The AAI believes that an assignee's repudiation of a RAND commitment as in the *N-Data* case – or as described in a March 2008 AAI petition to the FTC for action against patent holdup by Rembrandt, Inc. with respect to the nationwide conversion to digital television[20] – not only can violate the two prongs of Section 5 but can also constitute exclusionary conduct in violation of Section 2 of the Sherman Act, thereby enabling private as well as FTC enforcement action against it.

As detailed in AAI's Rembrandt petition, this view is supported by both policy and law. As a policy matter, an overly strict test for exclusionary conduct in this context would invite patent transfers that undermine standards development processes and thus harm consumers. A legal test for exclusionary conduct that requires deception or bad faith at the time a RAND commitment is given would unduly narrow available remedies and effectively countenance competitively harmful conduct. The FTC cannot pursue every alleged hold-up situation. In short, Section 5 does not provide sufficient deterrence

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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, 41 n. 247 (2006) (noting that patents are taken subject to existing licenses); *see also 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.").

[19] *See* Majority Statement of the Commission, *In re Negotiated Data Solutions LLC*, No. 0510094 (Jan. 22, 2008), *available at* http://www.ftc.gov/os/caselist/0510094/080122statement.pdf.

[20] Request for Investigation of Rembrandt, Inc. for Anticompetitive Conduct that Threatens Digital Television Conversion, American Antitrust Institute Petition to the Fed. Trade Comm'n, March 26, 2008, *available at* http://www.antitrustinstitute.org/files/AAI%20petition%20re%20rembrandt%20press%20release3.26.08_032520082005.pdf. The Commission has yet to respond to AAI's Petition.

of assignees from repudiating RAND commitments that they should be deemed to have assumed.

Most enforcement actions involving patent hold-up claims – public and private – have been based on some form of deception. But any conduct, whether or not deceptive, that subverts open-standards objectives can be held to be exclusionary within the meaning of Section 2. When a promise to do a future act is later repudiated, whether by the original promisor or a subsequent assignee, and that repudiation cannot be excused by accident or other legal justification, it is immaterial whether the intent not to honor the commitment is formed only after it is originally made. The anticompetitive consequences are no different from those in the more conventional scenario of an intent to deceive at the time of making the commitment. The reliance triggered by the giving of the commitment and the expectation that the commitment will be fulfilled become means of enabling anticompetitive hold-up outcomes. Thus, any subsequent action that upsets the reasonable expectations of the SSO members regarding their selection will have the same effect as deception or bad faith in the inducement. It should go without saying that if SSO members knew that the technology they selected would lead to patent hold-up, they would have chosen an alternative course.

One of the central lessons from *Allied Tube & Conduit Corp. v. Indian Head, Inc.*[21] is that the predicate conduct for an antitrust claim based on standard-setting abuse is not limited to deception – and may even literally comport with an SSO's rules: opportunistic conduct that subverts the standard-setting process and thereby harms competition can take various forms. Several authoritative commentators have explained that a bad faith repudiation or breach of a RAND commitment can be anticompetitive 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)."[22] Farrell and co-authors further state that antitrust enforcement may be appropriate where "a patent owner may make FRAND or similar commitments, then transfer relevant patents to another company that then claims not to be bound by those commitments."[23]

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[21] 486 U.S. 492 (1988).

[22] Joseph Farrell et al., *Standard Setting, Patents, and Hold-Up*, 74 ANTITRUST L. J. 603, 659 (2007).

[23] *Id.* at 648 n. 205.

Repudiation of a RAND commitment is similar to other opportunistic conduct held to be the basis for stating a claim of exclusionary conduct under Section 2.[24] For instance, the intentional breach of a binding commitment intended to restrain the acquisition and exercise of monopoly power has been held to constitute exclusionary conduct when found to have occurred as part of a scheme to acquire monopoly power.[25]

Repudiation of a RAND commitment to an SSO is also similar to the opportunistic conduct held to be exclusionary in *Eastman Kodak Co. v. Image Technical Services, Inc.*[26] Kodak's ex post policy change, permitting only Kodak-licensed service agents to purchase replacement parts for Kodak copiers, was held to be exclusionary because it foreclosed competition in copier repair services through a policy change that could not have been reasonably foreseen by Kodak's copier customers when they purchased the copiers, with attendant lock-in effects. The Court held that Kodak's opportunistic about-face after consumers had made significant and irreversible investments in its copiers could be a basis for a finding that Kodak engaged in exclusionary conduct under Section 2. No less should be true in the case of a patent assignee that repudiates a RAND commitment that it has assumed.

C. **Ex Ante Disclosure and/or Negotiation of License Terms**

The Commission asks how (a) a patent owner's ex ante disclosure of license terms and (b) ex ante discussions or negotiations of licensing terms affect the process of

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[24] *See, e.g.*, Sean Royall & Adam DiVincenzo, *The FTC's N-Data Consent Order: A Missed Opportunity to Clarify Antitrust in Standard Setting*, ANTITRUST, Summer 2008, at 83-92.

[25] *See Hewlett-Packard Co. v. Boston Scientific Corp.*, 77 F. Supp. 2d 189 (D. Mass. 1999) (where plaintiff alleged that in order to secure FTC approval of a proposed transaction, the defendant made express, binding commitments in a consent order to take certain actions to facilitate post-merger entry and competition, that after the merger was completed the defendant failed to live up to these commitments, and that the defendant thereby acquired monopoly power that it would not have possessed had it adhered to the terms of the consent order, the court held that such allegations, if proven, would support a Section 2 claim). In *Biovail Corp. Int'l v. Hoechst Aktiengesellschaft*, 49 F.Supp. 2d 750 (D.N.J. 1999), the court reached the same conclusion on similar facts. The FTC conditioned approval of a merger between Hoechst and Marion Merrell Dow (MMD) in part on the merged company's agreement to give Biovail a right of reference to data filed with the FDA in support of MMD's Cardizem, for approval of Biovail's competing generic drugs. Hoechst initially agreed and gave Biovail a right of reference, in a letter to the FDA, but it subsequently narrowed the scope of its commitment to the FDA. As a result, one of Biovail's applications for a drug to compete with Cardizem was denied for lack of supporting data; Biovail then sued Hoechst, alleging that it had intentionally reneged on its commitment to the FTC in order to win approval for its merger with MMD. The court held that if Biovail could show that the defendants narrowed the right of reference in order to keep Biovail's competing generic product from being approved, this would support a claim under Section 2 that defendants were willfully seeking to maintain or obtain monopoly power in the relevant market. *See id.* at 35.

[26] 504 U.S. 451 (1992).

choosing technologies for incorporation into the standard; to what extent "concerns about antitrust liability deter ex ante disclosure or negotiation of licensing terms"; and "'[w]hat considerations should shape a rule of reason analysis of joint ex ante license discussions or negotiations?"[27] As already indicated in the prior section, AAI believes SSOs should be encouraged or expected to require ex ante disclosure of license terms as a far more effective protection against ex post hold-up than currently prevailing and vacuous RAND commitment policies.

As DOJ recognized in its 2006 Business Review Letter on VITA's proposed policy of that kind,[28] such disclosures enable informed and meaningful choice among competing solutions during the course of the standards development process. "At a minimum, the disclosure of most restrictive licensing terms decreases the chances that the standard-setting efforts of the working group will be jeopardized by unexpectedly high licensing demands from the patent holder"; it is "an attempt to preserve competition and thereby to avoid unreasonable patent licensing terms that might threaten the success of future standards . . . ."[29] And there is no credible basis for resisting a requirement of this sort because of concern about antitrust liability in light of not only DOJ's VITA letter but also the analysis of it a year later in Chapter 2 of the 2007 DOJ-FTC Report on "Antitrust Enforcement and Intellectual Property Rights."[30] Ex ante "discussion" or "negotiations" warrant more caution as discussed below.

AAI agrees with the thrust of the agencies' analysis on the discussion/negotiation option as presented in the 2007 DOJ-FTC Report. As the agencies therein concluded: "Given the strong potential for procompetitive benefits, the Agencies will evaluate joint *ex ante* negotiation of licensing terms pursuant to the rule of reason."[31] Extensive caselaw supports rule of reason treatment for what is properly characterized as conduct analogous to joint purchasing of an input into a legitimate joint venture activity.[32] That said, however, any concerted activity of this kind among SSO participants presents some potential for antitrust mischief, both because the participants may be competing buyers of

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[27] 76 Fed. Reg. at 28038.

[28] *See* Business Review Letter from Thomas O. Barnett, Assistant Att'y Gen., U.S. Dep't of Justice, to Robert A. Skitol, Drinker Biddle & Reath LLP (Oct. 30, 2006), *available at* http://www.usdoj.gov/atr/public/busreview/219380.pdf.

[29] *Id.* at 9-10.

[30] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT & INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION 33-56 (2007), *available at* http://www.usdoj.gov/atr/public/hearings/ip/222655.pdf.

[31] *Id.* at 55-56.

[32] *See generally* Robert A. Skitol, *Concerted Buying Power: Its Potential for Addressing the Hold-up Problem in Standard-Setting*, 72 ANTITRUST L.J. 727 (2005).

licenses and because they may be competing sellers of standardized products or competing patent licensors. For this reason, an important element of the rule of reason analysis of any such joint discussion/negotiation should be consideration of process safeguards reasonably designed to minimize the risks of any such anticompetitive effects. We would accordingly encourage the Commission to promulgate guidelines or "best practices" suggestions on what effective safeguards may entail and, more generally, how any such joint discussion/negotiation activity can be structured in ways that comfortably pass the rule of reason test.[33]

We look forward to consideration of these and related issues at the Commission's upcoming standard-setting workshop. We would welcome discussing the AAI perspectives set forth herein with Commission officials whenever it may be useful to do so.

Sincerely,

Albert A. Foer
President

cc: Patrick J. Roach, Esquire
Suzanne T. Michel, Esquire

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[33] *See id.* at 739-42.