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Via Overnight Courier

Hon. Charles A. James
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U.S. Department of Justice
950 Pennsylvania Avenue, N.W.
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Hon. Timothy J. Muris
Chairman
U.S. Federal Trade Commission
Sixth & Pennsylvania Avenue, N.W.
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RE: U.S. Department of Justice Antitrust Division and Federal Trade Commission Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy

Dear Messrs. James and Muris:

The American Bar Association Section of Antitrust Law (the "Antitrust Section") is pleased to have the opportunity to submit this testimony in connection with the hearings being conducted jointly by the Antitrust Division of the Department of Justice ("DOJ") and the Federal Trade Commission ("FTC") on "Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy."

These views are being presented on behalf of the Antitrust Section only and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association ("ABA") and should not be construed as representing the position of the ABA.

The Significance of these Hearings

The Antitrust Section applauds this joint agency initiative to explore critical issues at the intersection of intellectual property and competition law and policy. Indeed, in the Antitrust Section's 2001 Report on "The State of Federal Antitrust Enforcement," prepared by a Section Task Force on the Federal Antitrust Agencies, the Antitrust Section urged the leadership of the federal antitrust agencies to encourage debate about the relationship between antitrust law and policy and intellectual property law and policy through public forums such as seminars and workshops.

We specifically urged the enforcement agencies to initiate a thorough public discussion of the optimal relationship between antitrust and intellectual property law and policies. We called for greater dialogue between the enforcement agencies, decision-makers in Congress and the Executive Branch, including those with responsibilities for intellectual property policy, and those in the business community who depend, more than ever before, on intangible intellectual property and innovation as competitive tools. We are therefore particularly pleased to see these hearings being conducted jointly by the DOJ and FTC, with the involvement of the Patent and Trademark Office, and testimony from business officials as well as from antitrust and intellectual property lawyers, economists and academics.

The Antitrust Section has itself focused substantial attention in recent years on issues at the intersection of antitrust and intellectual property law. The Antitrust Section has devoted resources to educating practitioners and also to furthering public policy debate regarding these issues principally through publications and programs. The Section has, for example, recently published a second edition of the *Federal Antitrust Guidelines for the Licensing of Intellectual Property: Origins and Applications* and published *Symposium: The Federal Circuit and Antitrust* in the Antitrust Law Journal. Recent Section programs have examined many of the same topics being addressed during these hearings, including the role of the Federal Circuit, refusals to deal, standard setting, and settlement of intellectual property litigation.[1]

The application of antitrust law to high-tech industries, and in particular the interaction of intellectual property law with antitrust enforcement, public and private, raise some of the most complex issues facing competition policy today. In today's knowledge-based "New Economy," the protection of intellectual property rights has, at the same time, taken on great importance to both large and small firms, making such

[1] We have also recently submitted comments jointly with the ABA Section of International Law and Practice and the Section of Intellectual Property Law on the European Commission Evaluation Report on the Transfer of Technology Block Exemption Regulation No. 240/96 on Technology Transfer Agreements Under Article 81.

issues even more significant. Indeed, in just the past decade, the number of patents, copyrights and trademarks has increased significantly. These developments impact not only high-tech industries such as the pharmaceutical, medical device and biotech industries and the computer hardware, software and telecommunications industries, but also traditional industries influenced by new innovations. The issues confronting such industries vary widely, for in some a patent represents a product, while in others hundreds and sometimes thousands of patents can be involved in the production of a single product. Evidence during these hearings suggests that in some industries innovation is closely tied to intellectual property protection while in others intellectual property is primarily secured as a defensive measure to ensure a company is not blocked from the market.

While the encouragement of innovation that is at the heart of intellectual property protection is fully consistent with the goals of antitrust policy, the intersection of these two regimes can raise complicated issues. These issues have heightened visibility because of recent enforcement actions by the agencies, and because of the determination by the United States Court of Appeals for the Federal Circuit that the Federal Circuit has broad jurisdiction over patent-related appeals in the federal courts, including antitrust litigation involving patent claims and defenses. Agency enforcement actions in this area have been among the most controversial, whether based on single firm conduct as in *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir.) (en banc), *cert. denied*, 122 S. Ct. 350 (2001), *Intel Corp.*, FTC Docket No. 9288 (1998), and *Dell Computer Corp.*, 121 F.T.C. 616 (1996), or concerted action as in *Schering-Plough Corp., Upsher-Smith Laboratories and American Home Products Corp.,* FTC Docket No. 9297 (2001), and *Summit Technology, Inc. and VISX, Inc.*, FTC Docket No. 9286 (1998). All of these cases, as well as DOJ's patent pooling business review letters,[2] involved high-technology industries in which the role of intellectual property and the impact of the conduct at issue and antitrust enforcement on innovation have been hotly debated. Public hearings are a useful tool for the agencies to explore criticisms of their enforcement theories as well as subjects that may warrant enforcement, outside the context of debate over individual cases.

The Relationship Between Antitrust and Intellectual Property Law

Most agree that both the antitrust and intellectual property laws provide important frameworks for the preservation and expansion of a competitive free market economy.

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[2] MPEG LA Business Review Letter (June 26, 1997); DVD 3C Business Review Letter (Dec. 16, 1998); DVD 6C Business Review Letter (June 10, 1999).

Intellectual property laws encourage large and small firms alike to invest in innovations that can create new industries or revolutionize existing markets, and innovation and dynamic competition is the source of long-term economic progress. Patents and copyrights, for example, encourage scientific advancement and creativity by allowing inventors to secure an economic return on innovation efforts by preventing free-riding for a limited term. Sometimes forgotten, however, is the fact that patents also require disclosure of inventions and thereby facilitate wide dissemination of knowledge and encourage individuals and firms to build upon earlier inventions or engage in cumulative innovation.

Antitrust law plays an important role in promoting consumer welfare by encouraging efficient utilization of resources and also by ensuring that consumers benefit from dynamic competition that enhances the pace and quality of innovation. As Learned Hand put it, "[p]ossession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; . . . immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress."[3]

Issues at the intersection of antitrust and intellectual property are not new. The courts have long struggled to reconcile antitrust enforcement with the statutory right to exclude under patent and copyright law.

We are fortunately past the time in which the antitrust community viewed antitrust and patent law as inherently in conflict, with the patent laws rewarding the inventor with a temporary "monopoly," frustrating the antitrust laws' goals to preserve competition and to prevent the creation or enhancement of monopoly power. There was a time, however, when regardless of their effect in the market, patents were characterized as "an exception to the general rule against monopolies."[4] It was not too long ago that one leading case reasoned:

> While the antitrust laws proscribe unreasonable restraints of competition, the patent laws reward the inventor with a temporary monopoly that insulates him from competitive exploitation of his patented art ...[T]he patent and antitrust laws necessarily clash. ...[T]he primary purpose of the antitrust laws – to preserve competition – can be frustrated, albeit temporarily, by a holder's exercise of the patent's inherent exclusionary power during its term.

SCM Corp. v. Xerox Corp., 645 F.2d 1195, 1203 (2d Cir. 1981), *cert. denied*, 455 U.S. 1016 (1982).

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[3] *United States v. Aluminum Company of America*, 148 F.2d 416, 427 (2d Cir. 1945).

[4] *Precision Instrument Mfg. Co. v. Automatic Maintenance Machinery Co.*, 324 U.S. 806, 816 (1945).

The view that patents were monopolies conferring market power to the detriment of competition led to restrictive views of the antitrust permissibility of intellectual property licensing practices, which culminated in the DOJ Antitrust Division enunciating guidelines during the 1970s that became known as the "Nine No-No's."[5] The Nine No-No's viewed as illegal per se: (1) requiring a licensee to purchase unpatented materials; (2) requiring a licensee to assign future patents; (3) restricting a purchaser of a patented product in the resale of the product; (4) restricting a licensee's ability to deal in products or services not within the scope of the patent; (5) a patent holder agreeing with a licensee not to grant future licenses to others without the licensee's consent; (6) mandatory package licensing; (7) royalties on the total sales price of products containing unpatented items; (8) restricting a licensee's sale of products made by use of the patented process; and (9) requiring a licensee to adhere to any price with respect to the licensee's sale of the licensed product.[6]

The modern view, as articulated in recent cases and most commentary, is that intellectual property laws authorize owners of intellectual property to exclude others from using that property. That is, increasingly it is recognized that intellectual property is like other forms of property. Patents do not necessarily create market power, and even when an invention is so successful that a patent does represent market power, there is no

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[5] In a September 21, 1972 address, the Deputy Assistant Attorney General, Antitrust Division, noted that the Department of Justice's nine rules had "quickly [become] known as the nine no-no's." B. Wilson, *Address Before Michigan State Bar Antitrust Section and Patent Trademark and Copyright Section* (Sept. 21, 1972), *partial text reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,125.

[6] See B. Wilson, *Patent and Know-How License Agreements: Field of Use, Territorial, Price and Quantity Restrictions, in* Antitrust Primer: Patents, Franchising, Treble Damage Suits 11, 12-14 (1970) cited in S. Anthony, *Antitrust and Intellectual Property Law: From Adversaries to Partners*, 28 AIPLA Quarterly Journal 1 (Winter 2000); B. Wilson, *Address Before Michigan State Bar Antitrust Section and Patent, Trademark and Copyright Section* (Sept. 21, 1972), partial text reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,125. Not long after they were announced, the Antitrust Division acknowledged that the Nine No-No's would not be given "wooden application," later suggested they were merely "signals of possible concern," and thereafter repudiated the entire list of concerns. *See* R. Andewelt, *The Antitrust Division's Perspective on Intellectual Property Protection and Licensing – The Past, the Present and Future* (July 16, 1985); A. Lipsky, *Current Antitrust Division Views on Patent Licensing Practices*, 50 Antitrust L.J. 515 (1981); K. Ewing, *Antitrust Enforcement and the Patent Laws: It is as Craftsmen that We Get Our Satisfaction and Our Own Pay*, Before the San Francisco Patent Law Association (May 5, 1979), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,128. B. Wilson, *Department of Justice Luncheon Speech Law on Licensing Practices: Myth or Reality* (Jan. 21, 1975). After the Nine No-No's were revoked, there were some who believed that there were "no No-No's" and that all of these practices were per se lawful. *See Report from Officialdom: 60 Minutes with Anne K. Bingaman, Assistant Attorney General, Antitrust Division, U.S. Department of Justice*, 63 Antitrust L.J. 323 (1994). Today, absent evidence of a naked restraint (e.g., price fixing, output restraints, market divisions, among horizontal competitors, and resale price maintenance), the practices should generally be analyzed under the rule of reason, as discussed below.

conflict between antitrust and intellectual property law, though antitrust issues may be raised by the exercise of such market power beyond the property right.

The view that the antitrust and intellectual property laws are in conflict follows from the mistaken presumption that the intellectual property laws create monopolies.[7] They in fact confer property rights, the right to exclude others, that may or may not give rise to monopoly power. A particular patent may offer one of several competing technological solutions and confer no market power on its owner, or it may offer the only solution and give its owner significant market power. In this respect, intellectual property is no different from real property that, likewise, confers a right to exclude trespassers. For example, real property such as a manufacturing plant or mine may be one of many competing plants or mines, or may be the sole plant producing a product or sole source of some mineral and may confer monopoly power to the extent there are no reasonably interchangeable substitutes for the product or mineral.

Antitrust and intellectual property laws are most often viewed today as complementary, both aimed at encouraging innovation and competition. As articulated in one leading case:

> When [a] patented product is so successful that it creates its own economic market or consumes a large section of an existing market, the aims and objectives of patent and antitrust laws may seem, at first glance, wholly at odds. However, the two bodies of law are actually complementary, as both are aimed at encouraging innovation, industry and competition.
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> [There is] a fine line between actions protecting the legitimate interests of a patent owner and antitrust law violations. On the one hand, the patent owner must be allowed to protect the property right given to him under the patent laws. On the other hand, a patent owner may not take the property right granted by a patent and use it to extend his power in the marketplace improperly, i.e., beyond the limits of what Congress intended to give in the patent laws. The fact that a patent is obtained does not wholly insulate the patent owner from the antitrust laws.

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[7] Ironically, the presumption continues to be shared by groups with antithetical views on the application of antitrust law to issues involving intellectual property. Opponents of antitrust enforcement sometimes argue that patents may at least at times, in fact, confer monopoly power, but contend that such monopolies are lawful and permit their owners to act with antitrust immunity. Some advocates of antitrust enforcement argue that where patents do grant market power there is a need to use antitrust law to prevent intellectual property owners from extending their power beyond the scope of the intellectual property at issue.

> When a patent owner uses his patent rights not only as a shield to protect his invention, but as a sword to eviscerate competition unfairly, that owner may be found to have abused the grant and become liable for antitrust violations.

Atari Games Corp. v. Nintendo of America. Inc., 897 F.2d 1572, 1576 (Fed. Cir. 1990).

Intellectual property law, by encouraging innovation and risk-taking, benefits consumers through the development of new and improved goods and services and production of goods and services at reduced cost. At the same time, antitrust law, by protecting competition as it is understood in its fullest dynamic sense, promotes innovation as well as price competition. Moreover, economics teaches that the effect of technological progress quickly swamps even significant static inefficiencies over time.[8]

Even in recent years, however, at least one notable antitrust official has suggested that there is a "tradeoff between intellectual property and antitrust" and has expressed concern that the balance has tipped to give intellectual property "inappropriate weight."[9]

Others, including the Court of Appeals for the Federal Circuit at times, have characterized patentees as having "immunity from the antitrust laws."[10] The CAFC has suggested that in order to fulfill its mission of promoting uniformity in the field of patent law, it is important to apply its own construction of patent law to the questions "whether and to what extent patent law preempts or conflicts with other causes of action," including antitrust law.[11]

Some who address the antitrust/intellectual property interface begin with a statement that the U.S. Constitution provides for intellectual property protection, insofar as Article I, Section 8, authorizes Congress "[t]o promote the Progress of Science and useful Arts, by securing for limited times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." It has even been suggested that, "[t]o the extent that the Patent Act and antitrust laws are based on dissimilar policies," competition regulators ought to be "cautious" in assuming that Congress intended "the distinctive policies of antitrust laws to trump those underlying the intellectual property system." It is

[8] *See, e.g.*, F.M. Scherer & D. Ross, *Industrial Market Structure and Economic Performance* 31, 613 (3d ed. 1990).

[9] R. Pitofsky, *Antitrust and Intellectual Property: Unresolved Issues at the Heart of the New Economy*, Before the Antitrust, Technology and Intellectual Property Conference (March 2, 2001).

[10] *Nobelpharma AB v. Implant Innovations, Inc.*, 141 F. 3d 1059, 1068 (Fed. Cir. 1998).

[11] *In re Independent Service Organizations Antitrust Litig.*, 203 F.3d 1322 (Fed. Cir. 2000), *cert. denied sub nom. CSU L.L.C. v. Xerox Corp.*, 531 U.S. 1143 (2001).

said that this is "especially so when one contemplates that the foundations for intellectual property protections are found directly in the United States Constitution."[12]

The antitrust laws have a constitutional stature no less than the patent and copyright laws. The antitrust laws are sanctioned by the Constitution's authorization to Congress in Article I, Section 8, to "regulate Commerce ... among the several States."[13] Thus, the Constitution authorizes Congress to adopt both antitrust and intellectual property laws, but does not mandate either.[14]

Moreover, the Sherman Act, while not passed until 1890, was based upon common law principles dating back hundreds of years.[15] Indeed, the Supreme Court has characterized the antitrust laws as "the Magna Carta of free enterprise," stating, "[t]hey are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms."[16]

The Court of Appeals for the Federal Circuit has itself held that "[i]ntellectual property rights do not confer a privilege to violate the antitrust laws."[17] As former Assistant Attorney General William Baxter once explained, one cannot violate other laws in the name of conditioning an intellectual property license: a "promise by the licensee to murder the patentee's mother-in-law is as much 'within the patent monopoly' as is the sum of $50.00, and it is not the patent law which tells us that the former agreement is

[12] J. Rogan, *Prepared Remarks, Before the Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy* (Feb. 6, 2002). *See also Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy,* Testimony of Q. T. Dickinson, (Feb. 6, 2002) at 56 ("The patent grant and the copyright grant are both constitutionally based, and they were among the first laws passed by the very first Congress sitting in Philadelphia").

[13] The Supreme Court has explained that when Congress enacted the Sherman Act, it "left no area of its constitutional power over commerce unoccupied," and "exercise[d] all the power it possessed." *Summit Health Ltd. v. Pinhas*, 500 U.S. 322, 329 n. 10 (1991) (quoting *U.S. v. Frankfort Distilleries Inc.*, 324 U.S. 293, 298 (1945), and *Atlantic Cleaners & Dyers Inc. v. U.S.*, 286 U.S. 427, 435 (1932)) (punctuation omitted).

[14] Indeed, as Justice Holmes once explained, "[the Fourteenth Amendment does not enact Mr. Herbert Spencer's Social Statics ... [and the] constitution is not intended to embody a particular economic theory." *Lochner v. New York*, 198 U.S. 45, 75 (1905) (Holmes, J., dissenting).

[15] *See, e.g.*, H. Thorelli, The Federal Antitrust Policy 12-35 (1954); W. Letwin, The English Common Law Concerning Monopolies, 21 U. Chi. L. Rev. 355 (1954).

[16] *United States v. Topco Associates, Inc.*, 405 U.S. 596, 610 (1972).

[17] *In re Independent Service Organizations Antitrust Litig.*, 203 F.3d 1322, 1325 (Fed. Cir. 2000), *cert. denied sub nom. CSU L.L.C. v. Xerox Corp.*, 531 U.S. 1143 (2001).

unenforceable."[18] Indeed, even though the Patent Act specifically authorizes the assignment of a patent to another by the patentee, an assignment of a patent to a competitor may violate the Sherman or Clayton Acts where the assignment constitutes unlawful monopolization or is part of an agreement to restrain trade or may substantially lessen competition, provided that the other elements of those violations can be proven.[19]

Issues at the antitrust/intellectual property interface are best resolved when each field has due respect for the other. Antitrust law must recognize and appreciate the legitimacy of intellectual property, the presumption of validity afforded to intellectual property rights and the right of intellectual property owners unilaterally to exclude others from utilizing such property. At the same time, intellectual property law must remember that representations to the Patent Office, certain restrictions in licensing agreements, cross-licensing and patent pools, patent acquisitions, patent settlements, and the use of intellectual property in standard setting may have antitrust implications. It should not be the rule that "[b]ecause a patent owner has the legal right to refuse to license his or her patent on any terms, the existence of a predicate condition to a license agreement cannot violate the antitrust laws."[20] That is, there is a fundamental difference between unilaterally refusing to license intellectual property to a prospective licensee and licensing only on the condition a prospective licensee take some action or refrain from taking some action that violates other law. Even where subject to the antitrust laws, however, most intellectual property licensing practices, as described below, are properly viewed as vertical and should be subject to rule of reason analysis. Any return to the era of the "Nine No-No's" would be wholly inappropriate.

The 1995 DOJ and FTC *Antitrust Guidelines for the Licensing of Intellectual Property* ("the *IP Guidelines*")[21] follow the modern view of the antitrust/intellectual property interface. They explain:

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[18] W. Baxter, *Legal Restrictions on Exploitation of the Patent Monopoly: An Economic Analysis*, 76 Yale L.J. 267, 277 (1966).

[19] *See, e.g., United States v. Singer Manufacturing Co.*, 374 U.S. 174 (1963) (transfer of patent part of broad monopolistic scheme); 35 U.S.C. § 261.

[20] *Townshend v. Rockwell Int'l Corp.*, 2000-1 Trade Cas. (CCH) ¶72,890 (N.D. Cal. March 28, 2000).

[21] The Antitrust Section does not consider the *IP Guidelines* to be a perfect statement of the appropriate antitrust analysis of intellectual property licenses, but does support the basic thrust of the *Guidelines*. The ABA Antitrust, Intellectual Property and International Sections provided comments on Draft Antitrust Guidelines for the Licensing and Acquisition of Intellectual Property in 1994. While many of the Sections' comments were taken into account before the final *Guidelines* were issued, some were not and this testimony is not intended to depart from those prior comments. For example, the Section has in the past expressed doubts as to whether the concept of an "innovation market" is a useful construct in antitrust analysis and believes that the concept is prone to abuse. Indeed, the Guidelines state that the agencies may "base the market share of participants in an innovation market on their share of identifiable assets or characteristics upon which innovation depends, on shares of research and development expenditures, or on

> The intellectual property laws and antitrust laws share the common purpose of promoting innovation and enhancing consumer welfare. The intellectual property laws provide incentives for innovation and its dissemination and commercialization by establishing enforceable property rights for the creators of new and useful products, more efficient processes, and original works of expression.... The antitrust laws promote innovation and consumer welfare by prohibiting certain actions that may harm competition with respect to either existing ways or new ways of serving consumers.

IP Guidelines ¶ 1.0. The 1995 *IP Guidelines* – and earlier sections of the 1988 DOJ *Antitrust Enforcement Guidelines for International Operations*, which dealt in part with international licensing issues – are to be praised for recognizing the complementary nature of antitrust and intellectual property, signaling a departure from the hostility to intellectual property expressed by both courts and the agencies in the past, and for providing the private sector with greater guidance on some nettlesome issues.

The 1995 *IP Guidelines* articulate three fundamental principles that we endorse. First, one should apply the same general antitrust principles to conduct involving intellectual property as to conduct involving any other form of tangible or intangible property. *IP Guidelines* ¶ 2.1.

The *IP Guidelines* at the same time do recognize that intellectual property has unique characteristics, such as ease of misappropriation and public goods characteristics that may impact antitrust analysis.[22] For example, the *Guidelines* recognize that "[i]ntel-lectual property typically is one component among many in a production process and derives value from its combination with complementary factors," "[s]ometimes the use of one item of intellectual property requires access to another," and "[l]icensing may promote the coordinated development of technologies that are in a blocking position." *IP Guidelines* ¶ 2.3. Significantly, as the *Guidelines* recognize, intellectual property "may in

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shares of a related product." IP Guidelines ¶ 3.2.3. We have previously submitted that there does not appear to be any empirical basis for assuming a correlation between size of budget or of "identifiable assets" and superior ability to innovate." We urged that "given the absence of empirical evidence and the unpredictable nature of innovation, an HHI-based standard would … seem particularly hard to justify" and suggested the agencies should "focus on the number of alternative sources potentially capable of innovation and qualitative factors that might better reflect innovative potential." Comments on Draft Antitrust Guide-lines for the Licensing and Acquisition of Intellectual Property § I.C.2.b (1994). *See also* ABA Section of Antitrust Law, Comments on the "Antitrust Guidelines for Collaborations Among Competitors" Issued in Draft on October 1, 1999 by the Federal Trade Commission and U.S. Department of Justice at 16 (Feb. 2000).

[22] *See generally* T. Jorde & D. Teece, *Rule of Reason Analysis of Horizontal Arrangements: Agreements Designed to Advance Innovation and Commercialize* Technology, 61 Antitrust L.J. 579 (1993).

some cases be misappropriated more easily than other forms of property" and that may "justify the use of some restrictions that might be anticompetitive in other contexts." *IP Guidelines* ¶ 4.1.2.

While competition principles are certainly relevant to intellectual property policy judgments, once those judgments are made, antitrust law should not be used to attempt to improve consumer welfare by changing the scope of intellectual property protection. Under the Constitution, judgments – such as whether patents should cover business methods or DNA sequences, how long patents or copyrights should last, and whether patents should be extended because of government regulatory delays in approving products – are generally left to the legislature. The judgment of the legislature regarding the appropriate balance of incentives for initial innovation, publication of innovations to foster follow-on innovations, and price competition, as embodied in intellectual property law, should be respected, so long as the legislature does not exceed Constitutional limits. It is not appropriate for antitrust enforcement agencies or the courts to attempt to improve the balance set by Congress by limiting intellectual property rights in particular cases where some party believes that there is over-protection. Antitrust decisions that limit intellectual property or that enhance the value of intellectual property to encourage innovation may upset the balance set by Congress. The way to change the balance is through amending legislation.

Second, the *IP Guidelines* explain that one should not presume that intellectual property necessarily confers market power despite the fact that courts historically have presumed that intellectual property gives an intellectual property owner a legal monopoly and market power. *IP Guidelines* ¶ 2.2. While there is a general consensus to support this view, there is, unfortunately, substantial older and some recent contrary authority,[23] including a split in the Supreme Court's latest pronouncement on the subject,[24] suggesting a need for legislation to overrule any residual presumption that intellectual property creates market power. We would support legislation that would make it clear that, in any

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[23] *See, e.g., MCA Television Ltd. v. Public Interest Corp.*, 171 F.3d 1265, 1277-79 (11th Cir. 1999) (block-booking per se illegal since the "licensor by virtue of its copyright is presumed to have 'economic leverage sufficient to induce his customers to take the tied product along with the tying item.'"); *Virtual Maintenance, Inc. v. Prime Computer, Inc.*, 11 F.3d 660, 666 (6th Cir. 1993) (licensee had market power in the derivative aftermarket for software support by virtue of its exclusive software license and a manufacturer's requirement that all suppliers use the licensed software), *cert. dismissed*, 512 U.S. 1216 (1994); *IBM v. United States*, 298 U.S. 131 (1936); *International Salt Co. v. United States*, 332 U.S. 392, 395 (1947); *United States v. Loew's, Inc*, 371 U.S. 38, 45 (1962) ("[t]he requisite economic power is presumed when the tying product is patented or copyrighted").

[24] *Compare Jefferson Parish Hosp. District No. 2 v. Hyde* 466 U.S. 2, 16 (1984) (dictum in majority opinion reaffirming presumption of market power, at least for tying claims); *Id.* at 37 n. 7(O'Connor, J. concurring) ("a patent holder has no market power in any relevant sense if there are close substitutes for the patented product").

action in which the conduct of an owner, licensor, licensee, or other holder of an intellectual property right is alleged to be in violation of the antitrust laws, such right shall not be presumed to define a market, to establish a market, or to establish monopoly power. Whether intellectual property confers market power requires a case-by-case inquiry. The American Bar Association House of Delegates has long endorsed such potential legislation in principle.[25]

It is worth noting that even where intellectual property does create market power, the exercise of that market power does not necessarily raise antitrust concerns. Illegal monopolization requires both the possession of monopoly power and "the willful acquisition … of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."[26] While antitrust law abhors the improper exercise of monopoly power because of the danger that it will lead to higher prices, lower output, poorer quality, and less innovation, it is fundamental that "[t]he successful competitor, having been urged to compete, must not be turned upon when he wins."[27]

Third, intellectual property licensing and cross-licensing can lead to integration with complementary factors of production and more efficient exploitation of the intellectual property and are typically pro-competitive. *IP Guidelines* ¶ 2.3. Thus, field-of-use, territorial, and other limitations in licenses that prevent free-riding are generally procompetitive, allowing a licensor to exploit its property efficiently and encouraging investments in commercialization and distribution of products.

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[25] In 1990, the House of Delegates of the American Bar Association adopted a policy position, which was reaffirmed in 2000, in support of H.R. 469, 101st Cong., a bill to provide that intellectual property rights shall not be presumed to define a market or to establish market power in actions under the antitrust laws. The ABA resolution states: "BE IT RESOLVED, That the American Bar Association favors in principle legislation such as H.R. 469, 101st Cong., 1st Sess. (1989) (Fish) and S. 270, 101st Cong., 1st Sess. (1989) (Leahy) which provides that intellectual property rights shall not be presumed to define a market or to establish market power in actions under the antitrust laws; RESOLVED, That the Association recommends such legislation cover specifically the licensing of or refusal to license such rights." *See* N. Rosen, *Intellectual Property Antitrust Protection Act of 1989, Before the Subcomm. on Economic and Commercial Law of the House Comm on the Judiciary*, 101st Cong., 2nd Sess., 59-70 (1990). In 1996, John R. Kirk, Jr., Chair-Elect of the ABA Section of Intellectual Property Law testified in support of H.R. 2674, which had essentially the same provisions. *See Intellectual Property Antitrust Protection Act of 1995 Before the House Committee on the Judiciary*, 104th Congress (May 14, 1996). Most recently, Charles P. Baker, Chair of the ABA Intellectual Property Law Section, testified in support of similar legislation. *See Market Power and Intellectual Property Litigation Before the Subcomm. on Courts, The Internet, and Intellectual Property of the House Comm. on the Judiciary*, 107th Cong., 1st Sess. 9 (Nov. 8, 2001).

[26] *See United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

[27] *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945).

Today, it is recognized that competitive concerns may arise where a licensing arrangement harms competition among entities that would have been actual or likely potential competitors in the absence of the license. Antitrust concerns are far less likely where licenses do not interfere with competition that would likely have taken place absent the license. *IP Guidelines* ¶ 3.1. A license between horizontal competitors (i.e., those that compete or potentially compete absent the license) may raise competitive concerns because the license may be used to conceal collusive behavior such as an agreement to allocate markets or may increase the likelihood of coordinated interaction in the market. The risk of such behavior depends upon market structure, including concentration, barriers to entry, and other market characteristics that bear upon the ability of market participants to collectively exercise market power. *IP Guidelines* ¶ 4.1.1. Where a license is vertical, rather than horizontal, the principal concerns are that the license may foreclose access to an important input or raise rivals' costs or facilitate coordination among competitors. *IP Guidelines* ¶ 4.1.1.

Proposed Changes to the Intellectual Property Guidelines

While there is widespread agreement today that antitrust and intellectual property law should be viewed as complementary, difficult issues remain at the intersection of the two fields and there is substantial uncertainty as to what conduct is acceptable. There is substantial uncertainty particularly with respect to agency enforcement positions regarding when an intellectual property owner may have a duty to deal, whether intellectual property may be an essential facility, disclosure and licensing obligations of firms involved in standard setting, and the appropriate analysis of intellectual property settlement agreements, including mergers or acquisitions among firms to settle intellectual property disputes. Our members and the clients they represent all recognize the value of clear guidance. Therefore, while perfect clarity in these areas may be elusive, we urge the agencies to move quickly to provide greater guidance in order to eliminate uncertainty as to their views.

We also urge several specific changes to the current *Intellectual Property Guidelines*.

First, the safe harbors in those *Guidelines* are inconsistent with the safe harbors in the April 2000 *Antitrust Guidelines for Collaborations Among Competitors* and should be updated and made consistent. The *IP Guidelines* identify a "safety zone" for intellectual property licenses, advising that the agencies will not, absent extraordinary circumstances, challenge a restraint in an intellectual property license agreement so long as the restraint is not one that is "facially anticompetitive" and normally warrants per se treatment (such as price fixing or market allocation), and so long as there are *four or more independent* *entities* that are not parties to the license that compete in the respective technology or innovation markets. *IP Guidelines* ¶ 4.3.

The more recent *Antitrust Guidelines for Collaborations Among Competitors* ("the *Competitor Collaboration Guidelines*") provide a slightly wider safety zone for research and development competition analyzed in terms of innovation markets:

> Absent extraordinary circumstances, the Agencies do not challenge a competitor collaboration on the basis of effects on competition in an innovation market where *three or more independently controlled research efforts* in addition to those of the collaboration possess the required specialized assets or characteristics and the incentive to engage in R&D that is a close substitute for the R&D activity of the collaboration.

Competitor Collaboration Guidelines at § 4.3. The *Competitor Collaboration Guidelines* also clarify that in determining whether independently controlled research and development programs are close substitutes, the agencies will consider a number of factors including: the nature, scope and magnitude of the research and development efforts; their access to financial support, intellectual property, skilled personnel or other specialized assets; their timing; and their ability – either alone or through others – to commercialize innovations successfully. *Id.*

The more recent *Competitor Collaboration Guidelines* purport to be consistent with the *IP Guidelines*, and indicate the *IP Guidelines* remain in effect, *id.* at n.4, while at the same time indicating the safety zones in the *IP Guidelines* relate to particular types of transactions, *id.* at n. 53, making reconciliation of the two safe harbors all the more important to avoid confusion.

A second troubling aspect of the *IP Guidelines* is that the safety zone analysis may be applied not only at the time of the license grant but also at a later date, and therefore parties may not be able to rely upon qualifying for safety zone treatment at the time of the license. The *IP Guidelines* state that the determination is to be "based on the factual circumstances prevailing *at the time of the conduct at issue*," and note that the conduct at issue may be the transaction giving rise to the restraint or the subsequent implementation of the restraint. Thus, the status of a licensing arrangement "may change over time." *IP Guidelines* ¶ 4.3.

While later evidence may be relevant to a restraint's reasonableness, a challenge ought to be based on a restraint's reasonableness at the time it is entered. Otherwise parties must continually reevaluate licenses and the most successful may be subsequently found illegal. Firms without market power that enter into an exclusive licensing arrangement to develop new and untested technology, bring together complementary expertise, and invest in a risky venture should not be found to have violated the antitrust laws because the technology proves to be successful and results in market power years later. Of course, once firms do gain market power, subsequent conduct must be examined in light of such market power.

The Antitrust Section commented on similar language in the *Competitor Collaboration Guidelines*, noting the policy tension between *ex ante* and *ex post* approaches to enforcement. *Compare SCM Corp. v. Xerox Corp.*, 645 F.2d 1195, 1208 (2d Cir. 1981) (legality of patent acquisition under section 2 evaluated by reference to market power at time of acquisition, not to market position developed subsequently), *cert. denied*, 455 U.S. 1016 (1982), *with Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal and Professional Publications, Inc.*, 63 F.3d 1540, 1554 (10th Cir. 1995) (following P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 711.2d, at 413 (Supp. 1994) (market "share that is relevant for determining whether the defendant can satisfy the 'dangerous probability of success' requirement of attempted monopolization should be either that which he possesses at the time of litigation or the largest share he possessed during the period of the alleged offense")), *cert. denied*, 516 U.S. 1044 (1996).[28]

The *IP Guidelines* do not even provide the limited comfort contained in the *Competitor Collaboration Guidelines*. There the agencies have suggested that while they will assess the competitive effects of an agreement "as of the time of possible harm to competition, whether at formation of the collaboration or at a later time," any assessment after formation will be "sensitive to the reasonable expectations of participants whose significant sunk cost investments in reliance on the relevant agreement were made before it became anticompetitive."[29] We previously suggested that clarification is needed as to how the "reasonable expectations" standard will be applied, particularly as to how the agencies will balance "reasonable expectations" against springing anticompetitive effects. We have expressed concern that the statement that the agencies will be "sensitive" to these issues is highly uncertain in its meaning and unlikely to offer much reassurance to businesses trying to evaluate risks in forming a venture.[30] The same is true of businesses entering licensing arrangements, and the *IP Guidelines* offer even less guidance.

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[28] *See* Comments of the Section of Antitrust Law Of the American Bar Association on the "Antitrust Guidelines for Collaborations Among Competitors" Issued in Draft on October 1, 1999 by the Federal Trade Commission and U.S. Department of Justice (Feb. 2000).

[29] *Competitor Collaboration Guidelines* § 2.4.

[30] *See* Comments of the Section of Antitrust Law Of the American Bar Association on the "Antitrust Guidelines for Collaborations Among Competitors" Issued in Draft on October 1, 1999 by the Federal Trade Commission and U.S. Department of Justice (Feb. 2000).

Firms ought to also be able to enter into licensing arrangements based upon reasonable, good faith expectations of patent validity and scope. Subsequent invalidation or narrowing of the intellectual property at issue should not render earlier licenses per se illegal unless the firms did not have a good-faith belief that the intellectual property at issue was valid and would have been infringed, or possibly, unless the firms do not adjust their licensing restrictions to reflect new information about the validity or scope of the intellectual property at issue. Definitive conclusions about infringement and validity usually occur, if at all, only after years of litigation. More frequently, there is never a definitive conclusion about the infringement or validity of the intellectual property at issue. Firms must make decisions about whether to grant licenses in a world of uncertainty, and should not face treble antitrust damages for conduct that they reasonably in good faith did not believe would diminish competition that would exist in the absence of the agreement. Further guidance would be useful to the effect that it is appropriate for business officials to rely upon good faith, reasonable determinations as to the likely outcome of patent litigation in entering license agreements.

Finally, the Section has previously suggested and continues to believe that an antitrust safety zone for restraints in license arrangements more permissive than the current 20% market share safety zone is appropriate for licensing between parties in a purely vertical relationship. We previously proposed the *Guidelines* state:

> Absent extraordinary circumstances, the Agencies will not challenge a restraint in licensing between parties in a purely vertical relationship if (1) the restraint is not of a type that normally warrants condemnation under the *per se* rule; (2) the licensor accounts for no more than 35 percent of each relevant market affected by the restraint; and (3) licensees subjected to the restraint collectively account for no more than 35 percent of each relevant market affected by the restraint.[31]

Both judicial precedent and the federal agencies' own policy statements in other contexts support adoption of a 35% threshold for potential market power concerns. *See, e.g., Jefferson Parish Hosp. District No. 2 v. Hyde* 466 U.S. 2, 26-27 (1984) (30% market foreclosure insufficient); DOJ/FTC *Horizontal Merger Guidelines* ¶ 2.211 (1997) (35% threshold for unilateral market power).

Report on the Court of Appeals for the Federal Circuit

As Chairman Muris noted in announcing these hearings, the Federal Circuit has had a significant impact on the development of antitrust as well as intellectual property

[31] *See* Comments on Draft Antitrust Guidelines for the Licensing and Acquisition of Intellectual Property at 17-18 (1994).

law.[32] Federal Circuit cases such as *Intergraph Corp. v. Intel Corp.*, 195 F.3d 1346 (Fed. Cir. 1999), and *In re Independent Service Organization Antitrust Litig.,* 203 F.3d 1322 (Fed. Cir. 2000), *cert. denied sub nom CSU L.L.C. v. Xerox Corp.*, 531 U.S. 1143 (2001), have drawn the attention of antitrust lawyers in the last few years. The Federal Circuit has exclusive jurisdiction over appeals from judgments in civil actions for patent infringement. Because patent and competition issues frequently arise together, the Federal Circuit also hears antitrust claims. As a result, the Federal Circuit has become an increasingly important participant in setting competition policy at the intersection of antitrust and intellectual property law.

Last fall, the Intellectual Property Committee of the Antitrust Section established a Task Force to study the consequences of the Federal Circuit's jurisprudence on its own jurisdiction and choice of law rules, in order to better understand the impact of these developments on the Federal Circuit's antitrust jurisprudence. The Task Force's study was sparked in part by a statement in the *amicus curiae* brief of the United States opposing certiorari in *CSU, LLC v. Xerox Corp.*, suggesting that the Supreme Court "allow the[] difficult issues [in that case] to percolate further in the Courts of Appeals." There was a perception among some observers that – given the Federal Circuit's expanding view with respect to its own jurisdiction – regional courts of appeals would seldom, if ever, consider the patent-antitrust issues raised in *CSU* and other cases. That is, rather than percolate in the various courts of appeals, future similar cases will likely be heard by the CAFC. Given the limited number of cases that the Supreme Court reviews, particularly in the absence of a circuit court split, the Federal Circuit, as a practical matter, may be the court of last resort and ironically may monopolize development of antitrust policy at the antitrust/intellectual property interface.

We have published as a Section publication and submit herewith the Report of the Task Force on the Federal Circuit, which examines the creation of the Federal Circuit, the development of its law and policy, the expansion of its jurisdiction, and the decisions of the court to apply its own law. This study is intended to trace the development of Federal Circuit law and its impact on competition policy. Our hope is that the study will contribute to the agencies' efforts to assess the significance and consequences of the Federal Circuit's increasing role in shaping antitrust law.

The Task Force report is organized in three sections. The first section provides an overview of the history of the creation of the Federal Circuit, including the legislative history regarding Congress' intent in creating the court. The legislative history reveals that Congress intended the Federal Circuit's jurisdiction to be narrowly circumscribed,

[32] T. Muris, *Competition and Intellectual Property: The Way Ahead*, Before the American Bar Association, Antitrust Section Fall Forum (Nov. 15, 2001).

but also anticipated that, in certain circumstances, the court would consider appeals related to antitrust issues. From the legislative history, it can be argued that Congress contemplated that the Federal Circuit would have some role in shaping antitrust law – in particular where antitrust claims are based on patent prosecution practices or certain types of licensing practices – but that Congress also expected the court to zealously guard against the expansion of that role beyond areas implicating the development of patent law.

The second section summarizes the current state of the law on Federal Circuit jurisdiction. It begins by examining the Supreme Court's decision in *Christianson v. Colt Industries Operating Corp.*, 486 U.S. 800 (1988), and then looks at Federal Circuit decisions addressing its jurisdiction over cases in specific circumstances: (1) where there is a patent claim combined with a non-patent claim or counterclaim; (2) where a patent claim was raised as a counterclaim in a non-patent case; (3) where patent claims were dismissed or withdrawn; (4) where patent claims and non-patent claims were separated for trial under Fed. R. Civ. P. 41(b); and (5) where a partial final judgment under Fed. R. Civ. P. 54(b) was entered. The report discusses the recent Supreme Court decision in *Holmes Group, Inc. v. Vornado Air Circulation Sys. Inc.*, 122 S. Ct. 1889 (2002), which held that the Federal Circuit does not have jurisdiction over appeals in cases in which the patent claim is raised in a counterclaim as opposed to the complaint. While that case did not involve an antitrust claim, its effect on the Federal Circuit's role in the development of antitrust law is potentially significant. This section of the report also discusses jurisdictional issues in cases involving non-patent claims that necessarily depend upon the resolution of a substantial question of patent law, such as cases involving contract disputes relating to patents and false statements regarding patent rights. The section concludes with a discussion of the Federal Circuit's jurisdiction to review orders of the Federal Trade Commission.

The third and final section of the report explores the development of the Federal Circuit's choice of law rules in antitrust cases (and the Federal Circuit's antitrust jurisprudence) both before and after *Nobelpharma AB v. Implant Innovations, Inc.*, 141 F.3d 1059, 1068 (Fed. Cir. 1998) (*en banc*), *cert. denied*, 525 U.S. 876 (1998), in which the court held that it would apply its own law to "an antitrust claim premised on stripping a patentee of its immunity from the antitrust laws." In examining the pre-*Nobelpharma* cases, the report discusses the fact that the Federal Circuit had the opportunity to "make" antitrust law long before its decision in *Nobelpharma*. In particular, it focuses on Federal Circuit cases in which there was no regional circuit law on the particular issue, and cases in which the court simply followed its own precedent rather than apply the law of the regional circuit. In addition, this section of the report also discusses antitrust claimants' relatively poor record before the Federal Circuit and whether that record reveals an antipathy toward antitrust principles or simply the weakness of the antitrust theories involved. The section concludes with an analysis of the Federal Circuit's treatment of antitrust issues after *Nobelpharma* and reviews a number of decisions that flesh out the court's view of antitrust law and its ability to apply its own law to key issues. These decisions include *C.R. Bard, Inc. v. M3 Systems, Inc.*, 157 F.3d 1340 (Fed. Cir. 1998), *rehearing en banc denied*, 161 F.3d 1380 (Fed. Cir. 1998), *cert. denied*, 526 U.S. 1130 (1999), *Midwest Industries, Inc. v. Karavan Trailers, Inc.*, 175 F.3d 1356 (Fed. Cir. 1999), *Intergraph Corp. v. Intel Corp.*, 195 F.3d 1346 (Fed. Cir. 1999), and *In re Independent Service Organizations Antitrust Litig.*, 203 F.3d 1322 (Fed. Cir. 2000).

Whether or not one agrees with the outcome of these cases – or with the broad dictum in the cases that some commentators have found troubling – one thing is clear: the Federal Circuit is having a significant impact on the development of antitrust law. That impact is the result of the combined effect of the court's expanding view of its own jurisdiction and its decisions to develop its own substantive antitrust law on patent-antitrust issues. Unless Congress, the Supreme Court, or the Federal Circuit itself acts to limit the court's discretion in these areas, the Federal Circuit's influence on the development of antitrust law will undoubtedly continue to be significant, potentially to the exclusion of other circuit courts.

Conclusion

We appreciate the opportunity to contribute to these important hearings and hope that this testimony and the enclosed Federal Circuit Task Force Report will be of assistance to the agencies.

Respectfully submitted,

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