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AIPLA TESTIMONY BEFORE
FEDERAL TRADE COMMISSION AND ANTITRUST DIVISION
ON ANTITRUST AND INTELLECTUAL PROPERTY ISSUES
April 10, 2002

On behalf of the American Intellectual Property Law Association, we welcome this opportunity to provide our association's views on antitrust and intellectual property protection in promoting innovation and competition. We offer our views on several specific topics that pertain to the interface between these two sets of laws and about which the Agencies solicited comments: the roles of antitrust law and intellectual property law in fostering innovation (Part II, below); unilateral refusals to license intellectual property (Part III); settlement of intellectual property disputes (Part IV); the role of the Federal Circuit in developing antitrust law in the intellectual property area (Part V); the scope of patents (Part VI); the lack of market power of intellectual property (Part VII); and the use of different types of licensing (Part VIII).

I. The AIPLA

Initially, let me give you a little background on our organization so that you can better understand the basis for our comments today. The AIPLA is a national bar association representing a cross-section of the intellectual property bar in the United States. Our membership includes attorneys who are in-house, private, government, and academic, and who represent a wide range of clients involved in all aspects of intellectual property licensing and protection. Our members, who number over 13,000, regularly work with diverse issues involving patents, copyrights, trademarks, trade secrets, and unfair competition law, as well as other fields of law affecting intellectual property. They advise large corporations, small companies, individuals, institutions, and government agencies. Our members represent intellectual property owners seeking to enforce their intellectual property rights, as well as those sued for infringing intellectual property rights. And they represent parties that allege antitrust violations and misuse of intellectual property, as well as those who defend against those charges.

Our members' clients are among the most innovative companies in the world. They are vitally interested in continuing to promote innovation in the United States and increasing the number of new United States jobs based on new technologies without violating our antitrust laws.

As a result, we believe that we have a balanced view of the role of intellectual property protection in the innovation and competition processes. We also believe that this balanced view extends to the respective roles of antitrust enforcement and intellectual property.

One of the stated purposes for which the AIPLA was formed is to aid in making improvements in the field of intellectual property, including the study of and commenting upon the laws protecting such property rights. It is in pursuit of this purpose that the AIPLA expresses its views today.

II. Roles of Intellectual Property and Antitrust Laws in Fostering Innovation

Our members have learned that business competition spurs innovation and they seek to preserve it. But they do not want to stifle innovation by making it harder or less rewarding to innovate or compete in the United States. We believe that intellectual property protection is essential to promoting innovation and investment in new technologies and that licensing this property is procompetitive.

The core element of intellectual property rights is in the limited right to exclude others from carefully circumscribed areas. Patents and copyrights protect investments in innovations and expressions, respectively, for only limited, specific periods of time. Trademark rights protect marks from identical and confusingly similar uses by others. State common law trade secret rights protect proprietary information, such as know-how, only until the information is no longer secret. All are limited in scope to specific inventions, expressions, or information, and only in the exceedingly rare case do they encompass an entire antitrust relevant market. And all protect against only limited types of infringing activities.

Contrary to the suggestion of one court recently,[1] an intellectual property right is not like a baseball bat, which its owner has the right to use. Intellectual property rights give their owner no right to make, use, sell, or copy the technology or expression that is protected by the rights. For example, inventions very often are improvements on earlier basic inventions made by others. If the owner of the intellectual property rights to the basic invention wants to exercise its exclusivity, that owner can stop the owner of the rights to the improvement from making, using, or selling the improved invention. Likewise, the owner of the rights to the improvement can stop the owner of the rights to the basic invention from making, using, or selling the improved invention. The intellectual property rights thus give only the right to exclude, not the right to use.

That exclusivity is the powerful driving force behind the incentives to innovate, to license, and to compete. Intellectual property protection encourages investment in development and use of innovations. Moreover, patents encourage public disclosure of inventions so that others can learn from and expand upon them. By affording exclusivity and protection,

[1] *United States v. Microsoft Corp.*, 253 F. 3d 34, 62 (D.C. Cir. 2001).

intellectual property laws spur competitors to innovate around the protected property and to make advances in alternative and often superior technologies. Further promoting competition, intellectual property rights very often are licensed to others.

We view the antitrust laws as providing complementary protection of competition and fostering innovation. The antitrust laws, in our view, serve their proper role by stepping in to curb excesses in the marketplace only when restraints on competition exceed their reasonable bounds. In so doing, they allow existing and would-be competitors the freedom to develop and market innovations to better compete.

Consequently, we view the two sets of laws as fully sharing common, not conflicting, goals and acting together in balance.

III. Unilateral Refusals to License Intellectual Property

Unilateral refusals to license intellectual property may implicate the interface between intellectual property protection and the antitrust laws. The essence of the intellectual property right is the right to exclude others from using or copying the intellectual property. Without that exclusivity, the intellectual property right is essentially meaningless. We also recognize that the antitrust laws provide limits on what people can do with their property when restraints on competition in the marketplace exceed reasonable bounds. The AIPLA does not believe that the unilateral act of refusing to license intellectual property should be the basis for imposing antitrust liability.

Our starting point is the right to exclude that the intellectual property laws provide. The Constitution explicitly provides that Congress shall have the power to "promote the Progress of Science and the useful Arts, by securing for limited Times to Authors and Inventors the *exclusive Right* to their respective Writings and Discoveries." U.S. Const. art. I. § 8, cl. 8 (emphasis added). Implementing that power, the Patent Code, 35 U.S.C. § 154, provides that a patent provides the "right to exclude others" from making, using, offering for sale, selling, or importing patented inventions. And Congress has specifically provided that refusing to license that exclusive right shall not be a basis for denying a patent owner relief or deeming the owner guilty of "misuse or illegal extension of the patent right." 35 U.S.C. § 271(d)(4). The Copyright Act, 17 U.S.C. § 106, likewise provides the "exclusive rights" to reproduce, prepare derivative works, distribute, copy, perform, and display various types of copyrighted works. The Trademark Act, 15 U.S.C. § 1114, similarly provides the right to exclude the use in commerce of registered marks or imitations of them where the use is likely to cause confusion or mistake, or to deceive. Trade secret law also provides the right to exclude wrongful users of trade secrets.

Thus, the right to exclude is the very essence of the intellectual property right. The Supreme Court has expressly recognized: "The heart of [the patent holder's] legal monopoly is the right to invoke the State's power to prevent others from utilizing his discovery without his consent." *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 135 (1951).

Some courts have differed on whether, and how, this principle should be applied where antitrust allegations are premised on a refusal to license intellectual property.

For example, many cases have held that the antitrust laws do not restrict the patent owner's right to refuse to license its rights within the scope of the patent grant. In that line, the Federal Circuit reaffirmed that "the antitrust laws do not negate the patentee's right to exclude others from patent property," and concluded that the Supreme Court had done "nothing to limit the right of the patentee to refuse to sell or license in markets within the scope of the statutory patent grant." *In re Independent Service Orgs. Antitrust Litigation*, 203 F.3d 1322, 1325, 1327 (Fed. Cir. 2000). Also in that line, *see*, for example, *Hartford-Empire Co. v. United States*, 323

U.S. 386, 432 (1945) (explaining that a patent owner "has no obligation either to use [the patent] or to grant its use to others").

The Federal Circuit has recognized, however, that the patentee's right to refuse to license is not unlimited and that a patent holder cannot use the patent right to refuse to sell a patented product to gain a monopoly in a market *outside* the scope of the patent. *See In re Independent Service Orgs. Antitrust Litigation*, 203 F.3d. at 1327-28. And other courts have held that the right to refuse to license intellectual property is not unlimited. For example, the First Circuit in *Data General Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1187 (1st Cir. 1994), concluded that "while exclusionary conduct can include a monopolist's unilateral refusal to license a copyright, an author's desire to exclude others from use of its copyrighted work is a presumptively valid business justification for any immediate harm to consumers," thereby precluding Sherman Act § 2 liability. The Ninth Circuit in *Image Techn. Svcs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1219 (9th Cir. 1997), accepted that presumption, but looked to the intellectual property owner's intent when refusing to license intellectual property to determine antitrust liability. Rejecting the Ninth Circuit's approach to intent, the Federal Circuit concluded that a patent or copyright owner's subjective intent in refusing to license its intellectual property is irrelevant to antitrust liability, as long as the competitive effect of the refusal is not extended beyond the scope of the statutory grant, or the refusal is not accompanied by fraud or sham litigation. *See In re Independent Service Orgs. Antitrust Litigation*, 203 F.3d. at 1327-29.

The AIPLA favors the Federal Circuit's approach. It reflects appropriate deference to Congress's determination that intellectual property protection—and the ability to exclude unauthorized use of intellectual property—promotes competition over the long run. The right to exclude—and thus the right to refuse to license—is an explicit statutory right given to the owner of intellectual property by Congress. We believe that no basis exists for conditioning the exercise of that right on a subjective inquiry into the intellectual property owner's motivation for refusing to license.

A rule that allows the presumption that a refusal to license was legitimate to be rebutted, particularly based on a subjective inquiry into intent, is contrary to a fundamental underlying purpose of the intellectual property system—creating incentives to innovate. A rule that would limit the right to exclude would greatly reduce the value of intellectual property. Moreover, such a rule would reduce that value by increasing uncertainty. It would make it far more difficult to dispose of antitrust claims based on a refusal to license via summary judgment. Consequently, an intellectual property owner's decision not to license would be more likely to be exposed to the inherent uncertainties of a jury trial.

IV. Settlement of Intellectual Property Disputes

The agencies also asked for views on competition issues that arise in the settlement of intellectual property disputes. Obviously, settlements are a form of agreement. Depending on the terms of the settlement and the relationship of the parties in the marketplace, they could raise antitrust issues similar to those raised by any other form of agreement. At the same time, settlements are an efficient means of resolving litigation and eliminating risk for owners of intellectual property and their potential competitors. Moreover, litigation settlements serve other important public policies, including conservation of judicial resources. We believe that antitrust rules relating to settlements need to accommodate all of these policy considerations.

A. Efficiency Benefits of Litigation Settlements

Litigation involves risk to both the intellectual property owner and the alleged infringer. The intellectual property owner risks the loss of a substantial investment in innovation if the intellectual property is declared invalid, unenforceable, or not infringed. The alleged infringer risks a substantial liability for the intellectual property owner's lost profits or lost reasonable royalties (which could be trebled if the infringement is found to be willful) and the loss of customer goodwill from having to withdraw its product from the market. And because litigation is a costly and inefficient way to resolve disputes, both parties risk the economic drain of litigation for as long as the litigation continues.

By reducing these risks, settlement of litigation will often confer benefits that serve the goals of competition and the antitrust laws. In the short term, eliminating risk through settlement may encourage the intellectual property owner to devote more resources to efforts to market its product and to invent improvements. It may also facilitate the efficient investment of resources by the alleged infringer. If the alleged infringer is granted a license, the elimination of litigation risk may justify a greater investment in marketing the product. If not licensed in the settlement, the infringer's resources are freed up to be devoted to more promising endeavors. Both parties usually benefit in the short term from terminating the financial drain of continued litigation.

In the longer term, a legal system that encourages intellectual property settlement agreements will promote certainty about the value of intellectual property rights and thus encourage investment in innovation. It should promote market entry and even challenges to intellectual property rights. A potential market entrant worried about possible infringement may be less inclined to take the risk of entry if it means a litigation “fight to the death” because settlement options are severely restricted by antitrust rules.

These pro-innovation, pro-efficiency effects of settling intellectual property litigation are all consistent with core antitrust and intellectual property law values.[2] In addition, settlement of litigation promotes values beyond those of the antitrust and patent laws. Courts strongly favor settlements, and particularly settlement of intellectual property cases, to conserve over-taxed judicial resources.[3]

B. Antitrust Analysis of Litigation Settlement Agreements

A few courts have recently held settlement agreements illegal under a *per se* rule.[4] We believe that applying a *per se* rule to litigation settlements is unwise and inappropriate.

Per se liability should be reserved for practices that "lack . . . any redeeming virtue."[5] The potential benefits to efficiency and innovation from litigation settlements described earlier

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[2] *See, e.g.,* Chairman Timothy J. Muris "Competition and Intellectual Property Policy: The Way Ahead," Remarks Before the American Bar Association Antitrust Section Fall Forum, November 15, 2001, at 2 ("IP law and antitrust law both seek to promote innovation and enhance consumer welfare"), *citing Atari Games Corp. v. Nintendo of America*, 897 F.2d 1572, 1576 (Fed. Cir. 1990) (patent and antitrust law "are actually complementary, as both are aimed at encouraging innovation, industry and competition.").

[3] "Public policy strongly favors settlement of disputes without litigation. Settlement is of particular value in patent litigation, the nature of which is often inordinately complex and time consuming. Settlement agreements should therefore be upheld whenever equitable and policy considerations so permit. By such agreements are the burdens of trial spared to the parties, to other litigants waiting their turn before over-burdened courts, and to the citizens whose taxes support the latter. An amicable compromise provides the more speedy and reasonable remedy for the dispute." *Aro Corp. v. Allied Witan Co.*, 531 F.2d 1368, 1372 (6th Cir. 1976); *see also Bradley v. Chiron Corp.*, 136 F.3d 1317, 1322 (Fed. Cir. 1998); *Foster v. Hallco Mfg. Co.*, 947 F.2d 469, 477 (Fed. Cir. 1991); *Speed Shore Corp. v. Denda*, 605 F.2d 469, 473 (9th Cir. 1979).

[4] *Cardizem CD Antitrust Litigation*, 105 F.Supp.2d 682, 700-06 (E.D. Mich. 2000), *appeal docketed*, No. 00-2483 (6th Cir. Dec. 19, 2000); *Terazosin Hydrochloride Antitrust Litigation*, 164 F.Supp.2d 1340, 1348-53 (S.D. Fla. 2000).

[5] *Northern Pac. Ry. v. United States*, 356 U.S. 1, 5 (1958).

suggest that *bona fide* settlements should not be subject to a *per se* rule. It would seem to be particularly inappropriate to apply a *per se* rule to conduct that the courts explicitly encourage.

An additional reason for not applying a *per se* rule to intellectual property litigation settlements stems from the competitive relationship of the parties. *Per se* violations usually involve horizontal agreements between actual or potential competitors.[6] But, as the Agencies' Intellectual Property Guidelines point out, "the Agencies ordinarily will treat a relationship between a licensor and its licensees . . . as horizontal when they would have been actual or likely potential competitors in a relevant market *in the absence of a license*."[7] Whether the alleged infringer would be able to compete absent a license is, of course, typically the central dispute. In order to apply a *per se* rule to an intellectual property settlement, a court must, in effect, assume that the intellectual property owner would lose the infringement suit—an assumption that no court is entitled to make without a trial of that issue.[8] For these reasons, we believe that, absent a fraudulent intellectual property right or a sham lawsuit or settlement, intellectual property settlements should be analyzed under the rule of reason, rather than any *per se* rule.

The starting point for a rule-of-reason analysis of an intellectual property settlement should be the range of possible outcomes in the litigation. At one extreme is the possibility that the intellectual property owner will win and the alleged infringer will be enjoined from

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6 Federal Trade Commission and U.S. Department of Justice, *Antitrust Guidelines for Collaborations Among Competitors*, §1.2 (April, 2000); Federal Trade Commission and U.S. Department of Justice, *Antitrust Guidelines For The Licensing of Intellectual Property*, §3.4 (April 6, 1995) (*IP Guidelines*). The one notable exception is resale price maintenance, where the parties are in a vertical relationship. Resale price maintenance is seldom a feature of intellectual property settlements.

7 *IP Guidelines, supra*, § 3.3 (emphasis added).

8 This is not to suggest that a court should undertake a trial of the merits of the infringement suit in the context of an antitrust suit, for to do so would effectively eviscerate the benefits of settlements.

competing by using the technology that is the subject of the intellectual property right until the right expires. At the other extreme is the possibility that the intellectual property owner will lose and the alleged infringer will be able to compete by using the technology immediately. The possibility that, had the litigation not been terminated by a settlement, the alleged infringer might have been enjoined from competing by using that technology significantly affects the antitrust analysis. Measured against that possibility of no competition by using that technology, restrictions in a settlement agreement do not necessarily represent a reduction in competition from the "but-for world" that would exist absent the settlement.[9]

We believe that the best way to analyze intellectual property settlements under the rule of reason is to adopt the following principle. Provisions in a settlement that fall within the range of possible outcomes in the litigation should be presumed lawful. Thus, an agreement that, without more, grants to an alleged infringer a license of the intellectual property rights at issue, which license is restricted in field of use, time (e.g., delayed entry), and/or geographic scope, should be presumed lawful. Also a settlement in which an alleged infringer essentially surrenders by stipulating validity and infringement and agreeing to stay off the market with that protected technology should be presumptively lawful. On the other hand, agreements relating to technology falling *outside* the scope of the intellectual property rights at issue should not fall within this presumption and so should be analyzed under normal antitrust principles.

Since by definition settlement provisions that fall within the range of possible litigation outcomes would represent a compromise of disputed claims, such a presumption would serve the

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[9] *See* H. Hovenkamp, *Antitrust Law*, vol. XII, ¶2046, at 265-66 (1999) (Agreements "whose outcomes are no more anticompetitive than a likely outcome of intellectual property litigation permitted to run its course" may be lawful "when used to settle a bona fide [intellectual property] dispute.").

judicial policy favoring settlements. It would also avoid the difficulty of speculating on the outcome of the litigation to re-create the “but-for world” that would be a necessary first step for analyzing apparent competitive effects under the antitrust laws.[10] Finally, the proposed presumption would avoid subsequent second-guessing as to the merits of the underlying patent suit by the Agencies and courts who, because they lack the parties’ access to the facts and the expertise, are less able than the parties to “get it right.”

This presumption should be subject to two exceptions consistent with existing case law. One is where the intellectual property right at issue has knowingly been obtained by fraud.[11] The other is where the litigation meets the test for sham litigation under *Noerr-Pennington* principles.[12]

Application of this presumption would foreclose several types of inquiry that would undermine the sound policies stated earlier. First, it would preclude an inquiry into the merits of the underlying infringement suit to re-create the “but-for world” necessary to determine apparent competitive effects. Foreclosing this inquiry preserves the certainty, elimination-of-risk, and cost-saving efficiencies promoted by settlements. Antitrust courts analyzing intellectual property settlements have so far not undertaken inquiry into the relative strength or weakness of the

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[10] *See* Commissioner Thomas B. Leary, "Antitrust Issues in the Settlement of Pharmaceutical Patent Disputes, Part II," Remarks to American Bar Association Antitrust Healthcare Program, at 2 (May 17, 2001). ("[I]n the words of our Intellectual Property Guidelines, the appropriate test [of competitive effect] is whether the settlement has an adverse impact on 'competition among entities that would [otherwise] have been actual or likely competitors.' The 'but for' world thus depends on whether the patent holder had the legal right to exclude the [alleged infringer] altogether, absent any settlement . . . .") (footnote omitted).

[11] *See Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.*, 382 U.S. 172 (1965).

[12] *Cf. Professional Real Estate Investors, Inc. v. Columbia Pictures Inds., Inc.*, 508 U.S. 49, 60-61 (1993).

underlying intellectual property claims. Nor should they. Such an inquiry into litigation probabilities is bound to be woefully imprecise. It would also appear to be inconsistent with the policies underlying the Supreme Court's decision in *Professional Real Estate Investors, Inc. v. Columbia Pictures Industries, Inc.*, 508 U.S. 49, 60 (1993), that parties have a right, unencumbered by the antitrust laws, to litigate any claim that is not "objectively baseless." If they have a right to litigate such claims, they ought to be able to settle them.

Also irrelevant under this approach would be an inquiry into motive or intent, which some courts have deemed relevant in the past. These would include a motive to exclude competition[13] or to avoid judicial determination of an intellectual property right's validity.[14] Evidence of a motive to exclude competition does not advance the antitrust analysis, since the very core of an intellectual property right is the right to exclude competitors. Nor does a motive to avoid an adverse judgment advance the antitrust analysis, since avoiding that risk is precisely why parties settle cases.

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[13] *See United States v. Singer Mfg. Co.*, 374 U.S. 174, 192-96 (1963) (motive to exclude foreign competition).

[14] *See Duplan Corp. v. Deering Milliken, Inc.*, 444 F.Supp. 648, 675-83, 686-87 (D.S.C. 1977) (settlement for purpose of avoiding possible ruling of patent invalidity); *United States v. Krasnov*, 143 F.Supp. 184, 202 (E.D.Pa. 1956) (same).

C. Proposals for Notification of Settlement Agreements

Proposals have recently been made to require notification to the Agencies of settlements of intellectual property litigation.[15] As the previous discussion has shown, intellectual property settlements are not the kind of pernicious agreements that deserve special scrutiny by government enforcement agencies. We therefore see no reason to single out these agreements and subject them to a reporting requirement that will burden both the settling parties and the Agencies forced to monitor such a program.

V. Role of the Federal Circuit in the Intellectual Property / Antitrust Arena

Among the primary reasons for the creation of the Federal Circuit were to introduce uniformity into patent law and resolve problems that had impaired the ability of the federal courts to deal with patent infringement cases. The Federal Circuit has been successful in resolving many of these issues by applying its own precedent to issues that pertain to its exclusive jurisdiction: patent infringement cases. Questions have arisen, however, regarding whether it should apply its own precedent to antitrust issues that arise in such cases.

In reviewing antitrust issues in patent infringement cases, the Federal Circuit normally applies the antitrust precedent of the regional court of appeals for the circuit in which the district court rendering the judgment is located. *See Nobelpharma AB v. Implant Innovations, Inc.*, 141 F.3d 1059, 1067 (Fed. Cir. 1998); *Loctite Corp. v. Ultraseal, Ltd.*, 781 F.2d 861, 875 (Fed. Cir. 1985). However, for issues that the Federal Circuit believes "clearly involve [its] exclusive

[15] In May 1997, the then head of the Antitrust Division proposed in very general terms a system of mandatory notification of "settlements of infringement disputes." Joel Klein, Acting Assistant Attorney General, Antitrust Division, U.S. Department of Justice, "Cross-Licensing and Antitrust Law," Address Before the American Intellectual Property Law Association, at 12-20 (May 2, 1997). Legislation is currently pending before Congress to require notification of patent litigation settlements between branded and certain generic manufacturers. *See* S. 754 (Leahy Bill); H.R. 1530, 107th Cong., 1st Sess. (2001).

jurisdiction," it applies its own precedent, rather than that of the regional circuit. *In re Indep. Serv. Orgs. Antitrust Litig.*, 203 F.3d 1322, 1325 (Fed. Cir. 2000). In that latter category, the Federal Circuit includes "conduct in procuring or enforcing a patent" and determines the antitrust liability of such conduct under its own precedent. *Id.* (quoted source omitted).

The AIPLA believes that the Federal Circuit's approach is correct. This approach can provide uniformity in application of the antitrust laws for patents that have nationwide scope and conduct that is not limited to one region of the country. Antitrust issues sometimes arise in the context of patent infringement cases. Disposition of those cases usually includes resolution of the antitrust issues and typically is not followed by a separate case involving only antitrust issues.[16] By applying a uniform antitrust standard in the infringement cases, uncertainty is reduced for patent owners, which fosters innovation, as discussed earlier. Moreover, applying its own precedent does not insulate the Federal Circuit from developments in antitrust law from other regional circuits. Those circuit courts of appeals each apply their own regional precedent. Yet they consider and adopt or reject developments from other circuits. The Federal Circuit does as well. *See, e.g., In re Indep. Serv. Orgs. Antitrust Litig.*, 203 F.3d at 1327 (considering and declining to adopt Ninth Circuit position on intent for antitrust liability for unilateral refusal to deal).

[16] Such a separate case would be appealed to other regional circuit courts.

VI. Scope of Patents

The Agencies asked for views on competition issues raised by the scope of patents and the procurement procedures under which they are issued. In our view, the scope raises competition issues, but none that the antitrust laws either do or should address, while the procurement procedures do not raise competition issues.

Certainly, the scope of patents can raise competition issues. Especially with basic inventions in a field, the broader the scope, the more incentive the patent owners often have to make inventions and the more incentive competitors often have to invent around. Narrower scope, on the other hand, may reduce incentives, because there may be no need to invent around to provide a good market alternative. Nonetheless, even narrow patents, especially on particularly successful products or methods, can spur competitors to invent new and improved alternatives.

Patents that are valid cover only new, useful, and non-obvious inventions. *See* 35 U.S.C. §§ 101-103. To the extent that inventions meet these criteria, they are within the scope of protection that Congress long ago decided to provide in implementing its constitutional power and directive to promote the progress of science and the useful arts. We see nothing wrong with the scope and these criteria, which enjoy the benefit of many years of continuing development, refinement, and balancing.

In our view, the scope of patents on various types of subject matter that recently have been criticized, e.g., business method patents, is neither too broad nor too narrow. We believe that our patent laws should not differentiate between the reward for making innovations in different subject matter. This year it may be business method patents that are criticized, next year biotechnology patents, the following year computer patents, the next year water treatment, the next . . . . The possibilities are endless. Tinkering with our patent laws to disfavor certain subjects would diminish the incentives to invest in those technologies for the long term, and may diminish the incentives to invest in other technologies that appear to be on the chopping block in future years.

Instead, we generally have faith in the self-correcting decisions by the courts. If a patent meets the statutory criteria, a court should sustain its validity. But if a patent is too broad because it, for example, either encompasses or is obvious over subject matter that was in the public domain, it should be held invalid. If a district court holds otherwise, the Federal Circuit can correct any mistakes. Moreover, if a court were to make a mistake in sustaining a patent, others in the industry can still challenge that validity, and if one challenge succeeds, the patent would be invalid as to all.[17]

In addition, since a patent rarely encompasses an entire antitrust relevant market, reasonable substitutes for the patented subject matter routinely exist. Consequently, patents themselves rarely adversely affect legitimate competition by precluding it in a market served by the patented subject matter.

Nor do we believe that numerous so-called patent "thickets" exist that preclude competitive challenges. With the assistance of skilled legal counsel, competitors usually can find their way around even large patent portfolios. Furthermore, many litigated cases involve allegations of infringement of multiple patents and challenges to their validity or infringement, demonstrating that competitive challenges exist despite numerous patents in a field.

[17] *See Blonder-Tongue Labs., Inc. v. University of Illinois Found.*, 402 U.S. 313, 350 (1971).

Consequently, while we believe that the scope of patents has competitive implications, we believe that scope should be left to the courts to develop as a matter of patent law. The scope should not be artificially altered to meet concerns of other bodies of law, such as antitrust. Instead, working with the scope of valid patents, the courts can balance the two complementary goals when they interface in particular cases.

We do not view the procurement procedures for patents as having antitrust significance or needing correction for antitrust reasons. The Patent and Trademark Office shoulders a tremendous responsibility in annually reviewing huge numbers of patent applications and deciding which deserve the patent reward. Over the years, the PTO has demonstrated its responsiveness to the changing needs of examining different types of subject matter. Unfortunately, recent Executive and Legislative Branch actions have severely undermined the ability of the PTO to meet the growing challenges it faces. Since 1992, the President and the Congress have combined to divert over $700 million of PTO fee revenues to other Federal programs. This diversion of revenue from the PTO has increasingly inhibited the PTO from routinely and promptly performing high quality search and examination of patent applications and establishing the electronic filing and processing of patent applications demanded by U.S. industry. Ensuring adequate support for the PTO to carry out its Constitutional mission could be one laudable outcome of these hearings. If it obtains proper funding, we believe it would have the ability to conduct a rigorous review of all patent applications.

Some have raised the question of whether procedures in the PTO, such as examiners' production quotas, favor granting patents that do not meet the statutory criteria. Examiners' quotas do not inherently favor either granting or rejecting patents. They only set an expectancy that a certain number of patent applications will be processed to one of two possible outcomes.

In our experience, the examiners in the PTO do not favor granting patents in inappropriate circumstances. Examiners routinely disallow patent applications and stick to their positions in the face of strong arguments from applicants.

VII. Lack of Market Power of Intellectual Property

The AIPLA believes that no presumption of market power should exist for intellectual property, in accordance with the position the federal antitrust agencies have taken.

The issue involved here is whether a presumption should exist that a patent, copyright, or other intellectual property right covering a particular aspect of technology conveys the power to raise or control prices or competition in any relevant market in which the protected technology competes. The issue arises because some courts, including the Supreme Court, have occasionally suggested that a patent presumptively confers market power. Nearly two decades ago in *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2 (1984), the majority opinion stated:

> [I]f the Government has granted the seller a patent or similar monopoly over the product, it is fair to presume that the inability to buy the product elsewhere gives the seller market power. Any effort to enlarge the scope of the patent monopoly by using the market power it confers to restrain competition in the market for a second product will undermine competition on the merits in that second market. Thus, the sale or lease of a patented item on condition that the buyer make all his purchases of a separate tied product from the patentee is unlawful.

Id. at 16 (citation omitted). In a concurring opinion, however, four Justices disagreed:

> A common misconception has been that a patent or copyright, a high market share, or a unique product that competitors are not able to offer suffices to demonstrate market power. While each of these three factors might help to give market power to a seller, it is also possible that a seller in these situations will have no market power: for example, a patent holder has no

> market power in any relevant sense if there are close substitutes for the patented product.

Jefferson Parish, 466 U.S. at 37 n.7 (O'Connor, J., concurring).[18]

Appellate court decisions are not uniform as to whether a patent or copyright presumptively confers market power on its owner or licensee. Although some appellate courts have rejected a presumption of market power for patents and copyrights,[19] others have not.[20] The Federal Circuit, which decides most appeals involving patents, i.e., those involving infringement claims, looks to the law of the regional circuit court of appeals for precedent on the general elements in antitrust issues arising in patent cases.[21] The Federal Circuit has indicated that it rejects any such market power presumption for intellectual property.[22] But it has done so following the precedent from the relevant regional court of appeals that also rejected such a

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[18] About 20 years earlier, the Supreme took a similar view in *Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.*, 382 U.S. 172, 178 (1965), explaining that "[t]here may be effective substitutes for the device which do not infringe the patent. This is a matter of proof . . . ."

[19] *See, e.g., SCM Corp. v. Xerox Corp.*, 645 F.2d 1195, 1203 (2d Cir. 1981); *A.I. Root v. Computer/Dynamics, Inc.*, 806 F.2d 673, 676-77 (6th Cir. 1986); *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665, 672 (7th Cir. 1985).

[20] *See, e.g., Ajir v Exxon Corp.*, Nos. 97-17032, 97-17134, 1999 WL 393666, *4 (9th Cir. May 26, 1999)(unpublished); *Digidyne Corp. v. Data Gen. Corp.*, 734 F.2d 1336, 1341-42 (9th Cir. 1984); *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792, 798 (1st Cir. 1988); *Duplan Corp. v. Deering Milliken, Inc.*, 444 F. Supp. 648, 673 (D.S.C. 1977), *aff'd in part, rev'd in part*, 594 F.2d 979 (4th Cir. 1979).

[21] *See Nobelpharma AB v. Implant Innovations, Inc.*, 141 F.3d 1059, 1068 (Fed. Cir. 1998); *Loctite Corp. v. Ultraseal, Ltd.*, 781 F.2d 861, 875 (Fed. Cir. 1985). As mentioned earlier, the Federal Circuit looks to its own precedent, however, with regard to "[w]hether conduct in procuring or enforcing a patent is sufficient to strip a patentee of its immunity from the antitrust laws . . . ." *Nobelpharma*, 141 F.3d at 1068; *see In re Indep. Serv. Orgs. Antitrust Litigation*, 203 F.3d 1322, 1325 (Fed. Cir. 2000).

[22] *In re Indep. Serv. Orgs.*, 203 F.3d at 1325 ("A patent alone does not demonstrate market power.")

presumption.[23] Thus, for patent-antitrust matters arising from district courts in which the regional circuit court of appeals would apply the presumption, the Federal Circuit may feel constrained to follow that approach.

A blanket presumption of market power for intellectual property bears no valid relationship to the real world. In all but the rarest of cases in our economy, products and methods compete with other products and methods that affect their market price. Thus, even if an intellectual property owner has the exclusive right to, for example, a particular product or method, that says nothing about how much competition that particular product or method faces from other products or methods that may be reasonably interchangeable and frequently are numerous.[24] Consequently, the AIPLA agrees with the concurring opinion of Justice O'Connor in *Jefferson Parish*, circuit courts of appeals that reject that presumption, and the Justice Department and Federal Trade Commission,[25] that no market power presumption should exist for

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23 The Federal Circuit in *In re Indep. Serv. Orgs.*, 203 F.3d at 1325, cited in support *Abbott Labs v. Brennan*, 952 F.2d 1346, 1355 (Fed. Cir. 1991) (applying law of Sixth Circuit, which rejected presumption); compare *Atari Games Corp. v. Nintendo of Am., Inc.,* 897 F.2d 1572, 1575-76 (Fed. Cir. 1990) (applying law of Ninth Circuit, which endorsed presumption).

24 While there undoubtedly are special challenges that arise when industry committees or consortia establish technical standards that are covered by patents, these issues can be met by rationalizing the standards process to make it more predictable and transparent, without making the ownership of a patent right a liability.

25 The Antitrust Guidelines for the Licensing of Intellectual Property issued by the U.S. Department of Justice and Federal Trade Commission, 1995 WL 229332 (April 6, 1995), provide, in pertinent part:

> The Agencies will not presume that a patent, copyright, or trade secret necessarily confers market power upon its owner. Although the intellectual property right confers the power to exclude with respect to the specific product, process, or work in question, there will often be sufficient actual or potential close substitutes for such product, process, or work to prevent the exercise of market power.

IP Guidelines, § 2.2

intellectual property.

Moreover, such a presumption would have negative effects. By skewing the rules to make it easier to prove an antitrust violation where intellectual property rights are involved than where such rights are not involved, such a presumption increases the risk and thereby diminishes the value of the intellectual property right to exclude. In diminishing that value, such presumption, for no justifiable reason, would decrease the incentives to develop and disseminate to others (e.g., through licensing) technology worthy of intellectual property rights protection. The AIPLA strongly believes, however, that the full incentives to develop and disseminate intellectual property should be preserved in order to stimulate and promote the greatest creation and use of technology in our economy, and thereby make our economy even more competitive.

Although only certain circuit courts of appeals have not rejected such a presumption of market power, an intellectual property owner may face the risk of being sued or having to sue in one of those circuits. Consequently, the value of the intellectual property is diminished as long as any court of appeals endorses such a presumption.

We are not aware of any judicial or other precedent holding that the mere ownership of any other type of asset creates a presumption of market power. We believe that Congress and the courts should permit intellectual property to enjoy the same market power tests applicable to other assets. Accordingly, the AIPLA believes that legislation should uniformly reject any market power presumption for intellectual property.[26]

VIII. Licensing Issues

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[26] See letter to Honorable Howard Coble, Chair, Subcommittee on Courts, the Internet, and Intellectual Property, November 28, 2001 (http://www.aipla.org/html/legislative/107/power.pdf).

The Agencies asked for information about the use of cross-licensing and patent pooling for the transfer or joint use of intellectual property. In the time available, we offer some generalizations and would be happy to further address particular aspects at the Agencies' request.

The frequency of cross-licensing often depends on the industry and the size of the parties. If there are major players in an industry, each of which sells similar products and has a substantial intellectual property portfolio of similarly valued intellectual property, the likelihood and necessity of cross-licensing may be high. When a company has a portfolio that is disproportionately valuable compared to those of others in the marketplace, cross-licensing is still possible, but the compensation may reflect the different values. One of the greatest hindrances to cross-licensing is the difficulty of determining the comparative values of intellectual property portfolios.

If there are many major players in a market, but one company creates a breakthrough invention and others cannot readily create non-infringing alternatives, less incentive to cross-license will exist. Cross-licensing also is less likely when an intellectual property owner has intellectual property that others want, but the owner does not need a license because it is at a different level in the manufacturing/distribution chain or holds the basic rights in the field.

Pooling acts somewhat like a cross-license, licensing intellectual property in a group with each participant contributing some rights. It is sometimes used where various individual companies, each having key contributions to an industry sector, need to work together to promote and sustain business within the sector.

IX. Conclusion

The AIPLA appreciates the opportunity to contribute to the FTC's and Antitrust Division's understanding of the dynamics of intellectual property and its benefits for promoting competition.

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