



# The Patent-Antitrust Interface: Are There Any No-No's Today?

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Antitrust law and patent law are legal tectonic plates – always in motion, occasionally converging, occasionally diverging, and occasionally moving in parallel relation. As patent suits have recently multiplied, the antitrust enforcement policies have again responded – for example, imposing pro-competition rules on patent case settlements, on abuses in standard setting situations, and on practices used to obtain patents in the first instance.

When the two disciplines' plates converge, we see the direct clash of the constitutional grant of a patent monopoly confronting the statutory edict against monopoly. When the plates diverge, we see that antitrust law has no bearing on many of the important patent doctrines of obviousness, anticipation, best mode, claims construction and the like. And when the doctrines transform – moving sideways in relation to each other – we see often compatible principles in royalty calculation, innovation promotion, and licensing practices.

At various times in the nation's legal history, one discipline or another has been dominant. The Supreme Court could say in 1902 that the "general rule" was the "absolute freedom in the use or sale of rights under the patent laws... The very object of these laws is monopoly." *E. Bennett & Sons v. National Harrow Co.*, 186 U.S. 70 (1902). But 60 years later, antitrust law treated intellectual property rights more skeptically, leading to perhaps the zenith of antitrust's dominance in 1970.

We will use that latter era as our discussion jump-off point, referencing a set of doctrines issued at the time when the antitrust tectonic plate was dominant, when patents and patent licensing practices – mostly of a vertical nature – were viewed with anti-competitive suspicion. It was the era of the "Nine No-Nos," articulated by the Antitrust Division in 1970. Over time, these per se illegal prohibitions succumbed to the free market thinking of antitrust enforcers in the Reagan and Bush administrations. Yet just when patent law appeared to be on a long run of domination, we are now again witnessing a renewed pushback against patents – a pushback led by the Supreme Court rulings, by defendants in suits brought by non-practicing entities, and by the Federal Trade Commission. Could a Reagan era antitrust enforcer ever have imagined that today's FTC would hold hearings on whether the assertion of weak patents in infringement litigation brought by "Non-Practicing Entities" (aka "trolls") could constitute unfair competition?

The two regimes are ever moving, often in conflict, and always creating new challenges for intellectual property and antitrust lawyers. What we shall observe is that the Nine No-Nos of the 1970's were a collective condemnation of larger, vertical patent licensing practices as per se illegal. That per se prohibition is absent in contemporary antitrust law. Today, vertical restraints – whether involved in a patent license or not – are never per se illegal. However, we do see in the Nine No-Nos some foreshadowing of practices that the modern antitrust enforcer may challenge – practices that use patent powers to extend market power. The Nine No-Nos asked the right question – how does a patent holder unlawfully extend the patent grant – but may not have provided the right answers. Today, an antitrust analysis requires more than a rote incantation of a patent to prove market power. A patent is important to consider, but is not determinative.

Let us proceed, then, to discuss some current antitrust issues looking through the lens of the Nine No-Nos. The Nine No-Nos were:

1. Tying of purchase of unpatented materials as a condition of a patent license;
2. Requiring the licensee to assign back or grant an exclusive grant-back license of subsequent patents obtained by the licensee;
3. Restricting the right of the purchaser of the product in the resale of the product;
4. Restricting the licensee's ability to deal in products outside the scope of the patent;
5. Promising a licensee that the licensor would not grant further licenses;
6. Mandating that the licensee take a "package license";
7. Imposing royalty provisions not reasonably related to the licensee's sales;
8. Restricting a licensee's use of a product made by a patented process; and
9. Requiring a minimum resale price for the licensed products.

## THE FIRST NO-NO: TYING THE PURCHASE OF UNPATENTED MATERIALS AS A CONDITION OF A PATENT LICENSE

This doctrine is known as the “anti-tying” doctrine. A tying arrangement, or tie-in, arises when a company places a condition on the sale, leasing, or licensing of one valuable thing on the licensee’s willingness to take some other – usually less desirable – product in addition. A critical first step in a tying case is to determine whether the “tying” thing evidences market power. Antitrust law will prevent a tie of unpatented goods to a patent license only when the licensor has market power in the patented product or patented process. In earlier years, a patent was presumed to bestow market power, facilitating the illegal tie-in. Now, just possessing a patent doesn’t prove market power – it proves only that you have a patent. *See, e.g., Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006).

In the intellectual property realm, tie-ins have repeatedly been subject to antitrust scrutiny, with unpredictable legal outcomes: a license to mimeograph machine technology lawfully conditioned on the purchase of ink and paper from the licensor (*Henry v. A.B. Dick Co.*, 224 U.S. 1 (1912)); the right to use patent machinery unlawfully conditioned on an obligation to purchase non-patented supplies (*United Shoe Machinery Corp. v. United States*, 258 U.S. 451 (1922)); and a license to a patented process involving the application of an unpatented chemical lawfully conditioned on the purchase that chemical from the patent owner (*Dawson Chem Co. v. Rohm & Haas*, 448 U.S. 176 (1980)).

Over the years, patent and antitrust law clashed in this area, with patent law dominant early in the 20<sup>th</sup> century, antitrust law dominant in the middle of the century, and a truce on the topic towards the end of the century, partially the result of legislation. In 1988, Congress amended the Patent Act to limit the scope of the patent misuse doctrine in tying cases:

No patent owner otherwise entitled to relief for infringement... shall be denied relief or deemed guilty of misuse... by reason of his having done one or more of the following:... (5) conditioned the license of any rights to the patent or the sale of the patented product on the acquisition of a license to rights in another patent for purchase of a separate product, unless, in view of the circumstances, the patent owner has market power in the relevant market where the patent or patented product on which the license or sale is conditioned.

35 U.S.C. § 271(d).

Today, we can say that the first “No-No” is of limited impact. By statute, the misuse doctrine will only apply if the licensor has market power in the relevant market for the patent or patented product. And mere possession of a patent no longer proves market power. And even with such market power, current case law suggests that there may be countervailing arguments to justify the tie. Two generally successful arguments justifying a tie are the use of tying arrangements to “meter” the value of the patent – the purchase of the unpatented tied product will be a measure of the value of the patented product or process to the user, as it measures the quantity of product made using the patented invention. A second defense is that tying an unpatented, but licensor-supplied, product to a patented invention is likely to result in a higher quality control, benefiting the licensor by preserving its reputation.

Perhaps the most prominent decision of recent currency exploring the tension between intellectual property law and antitrust law on this tying question is the U.S. Court of Appeals for the District of Columbia decision in *U.S. v. Microsoft*, 253 F.3d 34 (D.C. Cir. 2001), *cert. denied*, 534 U.S. 952 (2001), a case involving copyright rather than patent protection. Recall that, in that case, Microsoft had market power in the copyrighted Windows operating system and was accused of tying to that dominant system its own Internet Explorer web browser, to the exclusion of web browser competitors such as Netscape. The tie was accomplished in part by Microsoft comingling the code for both Internet Explorer and Windows in the same files. This comingling of Windows and Internet Explorer code was condemned under Section 2 of the Sherman Act case – an act prohibiting monopolies and monopolization. The appellate court also assessed the tying of the Windows operating system to the Internet Explorer web browser under Section 1 of the Sherman Act, with the appellate court eventually vacating and remanding the lower court’s finding of a violation. While the appellate court was comfortable in finding that the comingling of code constituted monopolization, it was less sure-footed on whether the comingled product constituted a per se illegal tie of two *separate* products – with shared code, was there really only one product? And in any event, a per se rule against tying was not warranted in a case involving bundling in platform software markets.

## THE SECOND NO-NO: REQUIRING THE LICENSEE TO ASSIGN BACK OR GRANT AN EXCLUSIVE GRANT-BACK LICENSE OF SUBSEQUENT PATENTS OBTAINED BY THE LICENSEE

The second “No-No” addresses a requirement in a license that the licensee assign back or give an exclusive grant-back of subsequent patents to the licensor. A grant-back obligates the licensee to provide the licensor with rights to the licensee’s intellectual property, often improvements that are related to the patent rights that are the subject of the license. If the licensee were to obtain a patent on the improvement and the licensor not have received a grant-back, the licensor might be unable to practice in the field without infringing the improvement patent. A grant-back allows the licensor to continue to compete, including using the most updated versions of his invention.

Why do grant-backs raise antitrust issues? If the grant-back is a full *assignment* or an *exclusive* license, then the licensee may not be able to practice the improvement and will not likely have sufficient incentive to improve the core technology. That disincentive might reduce competition. Of course, it is unlikely that anyone could practice the improvement without a license to the underlying patent owned by the licensor. To that extent, the grant-back does not really change the original patent owner’s market power in the original innovation.

Prior to the Justice Department’s articulation of this second No-No, the Supreme Court had approved, under the antitrust laws, license grant-backs. *E.g.*, *Transparent-Wrap Machine Corp. v. Stokes & Smith Co.*, 329 U.S. 637 (1947). There, the Supreme Court said that a grant-back was not *per se* unlawful, but rather subject to the rule of reason. Lower courts articulated several rule-of-reason factors to consider in evaluating whether a grant-back had anti-competitive effects, notably (1) the market power of the parties in the relevant market; (2) whether the parties were competitors; (3) whether the grant-back was exclusive or non-exclusive; (4) what rights, if any, the licensee retained to use the improvements; and (5) whether the grant-back was related to the scope of the licensed patents.

Following that precedent, the situations where a grant-back was deemed anti-competitive tended to be limited to instances where the grant-back was part of a broader pattern of obtaining intellectual property rights in order to obtain or sustain a monopoly. For example, in *United States v. General Electric Co.*, 82 F.Supp. 753 (D.N.J. 1949), the Court found the defendant had unlawfully attempted to monopolize by following the policy of acquiring every patent right in the market in order to exclude others, including the use of grant-back provisions to obtain rights to licensees’ improvements. Similarly, in *Kobe v. Dempsey Pump Co.*, 198 F.2d 416 (10th Cir. 1952), the accused party used grant-backs as part of a pattern of acquiring all patents related to oil pumps, constituting an attempt to monopolize.

For its part, the Justice Department has now disavowed this No-No as a per se prohibition. In its 1995 Antitrust Guidelines for the Licensing of Intellectual Property, the Justice Department concluded that, applying a rule of reason analysis, only *exclusive* grant-backs could be likely to be harmful, but that even then an important factor will be whether the patentee has “market power in a relevant technology or innovation market.” Moreover, one can argue that Congress has also addressed grant-backs in the 1998 amendments to the Patent Act, 35 U.S.C. § 271(d), concluding that, absent market power, a licensor will not be guilty of patent misuse if it “condition[s] the license of any rights to the patent... on the acquisition of a license to rights in another patent.”

This second No-No discussion does not address patent pools formed by horizontal competitors, which will be the subject of a separate No-No concerning “packaging” of patents. We do note, however, that a pattern of exclusive grant-backs, limiting the rights to practice the improvements to those entities participating in the pool, could be part of a challenge under Section 1 of the Sherman Act as a conspiracy to restrain trade by effectively denying new technology to competitors outside of the pool. *See, e.g.*, *United States v. Krasnov*, 143 F.Supp. 184 (E.D. Pa. 1956), *aff’d per curiam*, 335 U.S. 5 (1957). There, the consent of both of the cross-licensees in the patent pool was required to license third parties. Because the two patent pool members were the dominant competitors in the field of furniture slipcovers, the cross-license program was struck down as a restraint of trade. *See also*, *Matter of Summit Technology & Visx, Inc.*, Dkt. No. 9286 (FTC) (condemning agreement where two pool participants have joint veto power over the licensing of the pooled patents).

### THE THIRD NO-NO: RESTRICTING THE RIGHT OF THE PURCHASER OF THE PRODUCT IN THE RESALE OF THE PRODUCT

The third No-No addresses restrictions on the purchaser of the product in the resale of the product. It is important first to clarify the separate provisions of the Patent Act and the antitrust statutes pertaining to distribution of patented goods or goods made with patented products. Once we analyze the separate treatment under the respective regimes, we can assess whether there is any tension between them.

Under the Patent Act, the patent holder may grant and convey “an exclusive right... to the whole or any specified part of the United States.” Thus, the licensee may be limited to make and sell the product in limited territories – or to limited customers or in limited fields of use. But such rights are limited by the “first sale” or “exhaustion” doctrine first articulated in *Adams v. Berk*, 84 U.S. 453 (1873), and recently affirmed in *Quanta Computer, Inc. v. LG Electronics Inc.*, 553 U.S. 617 (2008).

In *Quanta*, applying patent, and not antitrust, doctrine, the Supreme Court restricted the ability of patentees to control all post-sale activities. There, LG Electronics licensed certain computer patents to Intel. Under that license, Intel could manufacture and sell microprocessors and chip sets embodying the patented technology. But the agreement specifically stated that no license was granted to Intel’s customers to combine (a) Intel products practicing the license patents with (b) non-Intel products – a license condition which was no doubt imposed by Intel on LG in order to force Intel’s customers to buy a full line of Intel components. Quanta purchased microprocessors and chip sets from Intel, aware of the condition prohibiting the use of non-Intel products. Nonetheless, Quanta manufactured computers using both Intel and non-Intel parts.

The case eventually made its way to the Supreme Court. That court held that LG could not assert the patent rights against Quanta which it may have had against its direct customer, Intel. Thus, at least under patent law, a patentee who has granted a licensee the right to make an article covered by the patent loses control of the article and cannot assert, under the patent laws, the right to impose further restraints on that article. A subsequent purchaser of the article from the initial purchaser who ignores a restriction imposed on the initial purchaser cannot be guilty of patent infringement. The Supreme Court in *Quanta* explicitly reserved the possibility that, under contract doctrines, LG might assert a claim against Quanta for breach of the condition imposed by Intel – perhaps under a third party beneficiary doctrine.

The restrictions on the right of the purchaser in the resale of the product are also triggered in the biotech field, notably with respect to bio-engineered products such as seeds that replicate. How will the law handle attempts to use the identical replicated product? Does exhaustion apply? Is there an exception for replicating products? Under patent law, use of copies of the sold product would seem to constitute patent infringement without triggering the exhaustion doctrine because the replicated seed had never been sold – only its parent had. *See, e.g., Monsanto Co. v. Scruggs*, 459 F.3d 1328 (Fed. Cir. 2006). The Supreme Court will take up this issue again this year in *Bowman v. Monsanto*. There, a farmer planted second generation seeds which he obtained from a grain elevator, not from the replication of seeds he acquired under license. The case could determine the bounds of exhaustion in patents involving replicating biologics.

Here is one example, then, where contemporary antitrust law may not be in conflict with patent law and may in fact be more permissive of a restraint. Under antitrust doctrine, a non-price vertical restraint imposed two layers down in the distribution chain would not likely violate the antitrust laws. Stated another way, the federal antitrust laws would not stand in the way of a *contract* action against a subsequent purchaser for violating a condition on resale, and would not likely find the vertical restraint to be anti-competitive.

This discussion does not touch on the special rules for resale *pricing* found in both patent and antitrust regimes, the subject of another No-No.

## THE FOURTH NO-NO: RESTRICTING THE LICENSEE'S ABILITY TO DEAL IN PRODUCTS OUTSIDE THE SCOPE OF THE PATENT

The fourth No-No articulated by the Justice Department addressed restricting the licensee's ability to deal in products outside the scope of the patent. This No-No principally covered the agreement of the licensee, as part of the condition to receiving the intellectual property, to refrain from dealing in the goods of others who may sell competitive goods or services to those offered by the licensor. In antitrust parlance, it is a commitment to "exclusive dealing." Like all vertical restraints, this restraint is now assessed under the antitrust laws under the rule of reason. The *per se* effect of a No-No rule is long-gone. It is likely to be held anti-competitive only if there has been a substantial foreclosure of opportunity to the licensor's rivals. Factors that an antitrust court would consider are (1) sufficient market power by the licensor to give it the ability to impose the restraint; (2) whether the firms accepting the exclusivity obligation constitute a significant portion of the consuming market; and (3) the duration of the exclusivity.

Decades ago, these kinds of exclusive dealing provisions in contracts were often condemned under the antitrust laws, *e.g.*, *Standard Oil of California v. United States*, 337 U.S. 293 (1949) (prohibiting refiner obligation that dealers sell only Standard Oil-branded gasoline); *United Shoe Machinery Corp. v. United States*, 258 U.S. 451 (1922) (prohibiting exclusive dealing clauses found in leases of patented shoe manufacturing machinery). *See also*, *FTC v. Motion Picture Advertising Service Co.*, 344 U.S. 392 (1953) (agreement not to license film from rival licensor deemed anti-competitive where 75 percent of industry covered by such clauses). More recently, aspects of Microsoft's licensing of its intellectual property were criticized by the courts, notably a per processor licensing provision which obligated an original equipment manufacturer to pay a license fee for every computer it manufactured, regardless of whether that computer loaded the Microsoft Windows operating system. But the Microsoft cases are distinguished by the fact that Microsoft had market power in the operating system. The use of the per processor clause – in practical effect an exclusive dealing clause – allowed Microsoft to perpetuate that power, and hence was part of a Section 2 monopolization campaign.

The current vitality of this No-No may be found, by mirror image, in certain of the standard setting antitrust cases. In the paradigm standard setting case, a company participates in an industry-wide effort to establish a standard for interoperability or compatibility. That organization likely has a rule requiring that patents be disclosed and that a patent holder agree to license the patent under fair, reasonable and non-discriminatory ("FRAND") terms. Later, after the standard setting organization has adopted the standard, the participant asserts a patent claim covering part or all of the standard, having failed to disclose that intellectual property previously. The economic effect of having one's technology embedded in a standard is akin to exclusive dealing – someone wishing to market a product compatible with an industry standard must use a technology covered by the patent holder's technology. The fact that the patent is embedded in an industry standard is, as in the Microsoft case, some evidence of market power. Because other technology may not be available in the case of an industry-wide standard, the patent owner has committed a No-No – it has obtained exclusivity.

The analogy is not perfect, in that the remedy for this antitrust violation is not necessarily to break the exclusivity provision but, rather, to impose a FRAND royalty remedy. Recently, the Federal Trade Commission has announced its enforcement intentions, under Section 5 of the Federal Trade Commission Act prohibiting unfair methods of competition, to force companies holding standard essential patents ("SEPs") to refrain from seeking injunctions and to honor their prior commitments to offer FRAND licenses. The FTC recently brought enforcement proceedings against Robert Bosch GMBH ("Bosch") for seeking injunctions based on two patents declared essential to industry standards. The FTC believed that the mere act of seeking injunctive relief based on FRAND-committed patents was an unfair method of competition. For its part, the Justice Department, in its public policy advocacy has stated similar enforcement intentions:

One concern is that a patent holder may demand licensing terms that are not consistent with this FRAND promise, and couple that demand with a threat of an injunction or other exclusionary relief. This would have the ultimate effect of undermining competition and the procompetitive benefits of the standard setting process.

"The role of standards in the current patent wars," speech by Fiona M. Scott-Morton, December 5, 2002.

In early 2013, the FTC reached a consent decree settlement with Google, whereby Google agreed to allow competitors to have access to critical SEPs on FRAND terms, and will not – save for limited circumstances – seek an injunction to ban practice of the technology. The settlement also describes the process Google must follow in establishing FRAND terms – notably arbitration or judicial process in lieu of an injunction proceeding.

Days later, the Justice Department and the U.S. Patent and Trademark Office issued a joint policy statement, mirroring the Google settlement: no injunctions where the patent holder has agreed to a FRAND obligation and the potential licensees are ready, willing and able to cut a deal.

#### THE FIFTH NO-NO: PROMISING A LICENSEE THAT THE LICENSOR WOULD NOT GRANT FURTHER LICENSES

The fifth No-No covered a licensor's agreement not to grant further licenses. In effect, the patent owner is telling its customer that the customer will not have any other competition, at least with respect to the patented technology. Antitrust treatment of such exclusive license has generally been favorable over the years. For example, in *Packard Motor Car Co. v. Webster Car Co.*, 243 F.2d 418 (D.C. Cir. 1957), the court upheld Packard's termination of dealers in order to maintain an exclusive dealership with a third, concluding that, despite the strength of the Packard brand, Packard did not possess market power in the overall automobile market and thus an exclusive dealership was not anti-competitive.

How does this No-No manifest itself in today's patent/antitrust interface? An imperfect analogy may be made to settlements reached between generic and brand name drug companies in Hatch-Waxman Act cases. Under that regime, the first-to-file generic applicant for a branded drug has a period of exclusivity in which no other generic may market the drug, once any patent battles have been resolved. As part of a settlement of a generic-branded patent dispute, the settling parties may agree that the generic will retain its exclusivity rights under the law but not assert them in the marketplace. That is, the exclusivity may stand to keep other generics off the market, but the lead generic will promise not to sell, perhaps in exchange for a "reverse payment" from the patent owner. The Supreme Court has recently agreed to step into this area, as there is a split of circuits on whether or not reverse payments are presumptively illegal. In *Federal Trade Commission v. Watson*, the Supreme Court could establish the standard for assessing the legality of Hatch-Waxman "reverse payment" settlements.

The FTC has lead this antitrust enforcement charge, asserting that reverse payments are inherently suspect and that a generic drug company may not barter the exclusivity rights bestowed by the Hatch-Waxman Act. The development suggests that this "No-No" banning exclusivity may still have life, at least in a context of a reverse payment settlement that includes the generic company preserving its exclusivity rights *vis-à-vis* other generics, while refraining from actually entering the market.

#### THE SIXTH NO-NO: MANDATING THAT THE LICENSEE TAKE A "PACKAGE LICENSE"

The sixth No-No prohibits mandatory "package" licenses. The concept is akin to a tying arrangement, discussed in the first No-No. But rather than tying a product to an intellectual property license, a package involves combining multiple intellectual property rights into a package. One historic example of mandatory packages is block booking of motion pictures. See, e.g., *United States v. Loew's Inc.*, 371 U.S. 38 (1962); and, more recently, *Six West Retail Acquisition, Inc. v. Sony Theatre Management*, 2000 W.L. 264295 (S.D.N.Y., March 9, 2000). Bundling may involve (a) a single holder of intellectual property imposing the bundle as a vertical restraint; or (b) as has become quite common in standard setting activities, the pooling of patents by horizontal competitors.

With respect to the former, a vertical restraint, bundling will only be illegal under a rule of reason analysis where there is coercion, where there are in fact separate divisible intellectual property rights, where the licensor has market power in the desired intellectual property right, and where there is some evidence of harm to competition. Examples of competitive consequence would be foreclosure of competitors in the tied product market. See generally *Microsoft, supra*. The Antitrust Guidelines, issued in 1995, abandoned this licensing practice as a per se No-No in a vertical context and suggested instead that an intellectual property package is likely to raise antitrust concerns only if there is injury to competition that would otherwise have occurred without the bundle.

In the patent pool area text – a horizontal context – the sixth No-No has more merit, particularly where the pool includes intellectual property rights that are not complementary to each other but in fact are substitutes for one another. Patent pools are common in the consumer electronics industries, notably with respect to DVDs and MPEG format, and are increasingly used in the pharmaceutical industry. See generally *Princo Corp. v. ITC*, 616 F.3d 1318 (Fed. Cir. 2010) (*en banc*). The Department of Justice and FTC Intellectual Property Guidelines address patent pools and acknowledge that they can be pro-competitive in certain circumstances but anti-competitive in others. A recent suit challenging the DVD patent pool was dismissed at the motion to dismiss phase under *Twombly* where, according to the district court, the plaintiff did not satisfactorily allege that the

patent pool in fact was anti-competitive. *International Norcent Technology v. Koninklijke Philips Elec. N.V.*, 2007 W.L. 4976364 (C.D. Cal. 2007).

The DOJ FTC Guidelines point to two anti-competitive consequences of patent pools: (1) where a potential competitor is denied access to the patents dedicated to the patent pool, thereby preventing competition; or (2) using a patent pool to impose price and/or quantity restraints. In the latter case, the government will look to whether the intellectual property dedicated to the pool is complementary or substitutable and, if substitutable, only one of the technologies is licensed by the pool.

The 2010 *Princo en banc* decision, arising in the context of a patent pool, was the most significant case in decades on patent misuse as a limit on patent enforceability. Historically, patent misuse was largely defined by antitrust principles – and sometimes was broader. *E.g., Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100 (1969) (royalties on products not covered by a patent could be misuse, but probably not an antitrust violation). *Princo* narrows patent misuse to a subset of anticompetitive practices limited to expanding the scope of the patent – contrasted with earlier patent misuse cases which addressed the use of a patent to exclude rivals.

The *Princo* case started as a patent infringement case brought at the ITC by Philips against Princo. The patent was part of a patent pool created by Philips, Sony, Ricoh, and Taiyo to develop compact disc standards.

Princo defended the infringement suit by alleging patent misuse in the aggregation of too many patents in the pool, not all of which were essential to the standard. By including non-essential, but potentially competitive, technology in the pool and limiting access to that technology outside the pool, Philips and others committed patent misuse, Princo asserted.

When the case was eventually resolved by the *en banc* court, the patent misuse doctrine was deemed inapplicable to the alleged agreement preventing the licensing of the “non-essential” competing technology outside of the pool. Rather, the misuse would only attach to conduct taken to leverage the asserted Philips patent beyond the scope allowed by the Patent Act.

#### THE SEVENTH NO-NO: IMPOSING ROYALTY PROVISIONS NOT REASONABLY RELATED TO THE LICENSEE'S SALES

The seventh No-No pertains to royalty provisions not reasonably related to the licensee's sales. This No-No captures a number of practices considered by the courts over the years as problematic under the antitrust laws, notably (1) agreements that call for the payment of royalties on goods that are unpatented or on which the patents have been found to be invalid; (2) agreements requiring royalties paid on output, whether covered by the patent or not; (3) agreements that call for royalties even after a patent has expired; and (4) other miscellaneous royalty provisions thought to expand the scope of the patent. Historically, under patent law, a license which demands royalties on products “which do not use the teaching of the patent” may be unlawful. *Compare Automatic Radio Manufacturing Co. v. Hazeltine Research, Inc.*, 339 U.S. 827 (1950) (permitting royalties based on the licensee's total revenues from sale of radios, including radios which did not include any patent covered by the license) *with Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100 (1969) (“[T]he patent's leverage may not... be used to garner as royalties a percentage share of the licensee's receipts from sales of other products....”) The *Zenith* opinion distinguished the *Automatic Radio* decision as one where the royalty based on output was agreed upon “voluntarily” for the convenience of the parties. That is, an all output royalty provision cannot be imposed *coercing* the patent owner, under *Zenith*.

As noted previously, this issue arose in the government's long and avid pursuit of Microsoft, whose licensing practices included, among other things, charging a per processor fee regardless of whether the Microsoft operating system was in fact used. In settling the case, Microsoft agreed to drop the per processor fee and to charge a license fee only for products that actually carried the Microsoft operating system.

A separate concern is a license which imposes a royalty on products even after the patent covering the products has expired. In *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), the Court considered a royalty agreement where royalty payments were to run beyond the time of the patent's expiration. The Court viewed the license as “a telltale sign that the licensor was using the licenses to project its monopoly beyond the patent period.” *Id.* at 32. Subsequent lower court cases have criticized *Brulotte* but felt compelled to follow it. *E.g., Scheiber v. Dolby Laboratories, Inc.*, 293 F.3d 1014 (7th Cir. 2002), *cert. denied*, 537 U.S. 1109 (2003); *Zila, Inc. v. Tinnell*, 502 F.3d 1014 (9th Cir. 2007).

This No-No arguably also covers a situation in which a patentee continues to seek royalties for patents that have been declared invalid. *See, e.g., Chromalloy American Corp. v. Fischmann*, 716 F.2d 683 (9th Cir. 1983). The

enforcement of invalid patents has given rise recently to novel antitrust suits. For example, in late 2012, a federal court jury found 3M in violation of federal antitrust laws for its efforts to enforce two fraudulently obtained patents against the plaintiff, a competitor to 3M in the market for oil-resistant and oil-proof respirators and filtration media used in those respirators. *See, e.g., Transweb LLC v. 3M Innovative Properties Co. et al.*, Case No. 2:10-cv-04413 (D.N.J.). The underlying complaint focused on invalid and fraudulently obtained patents, as well as sham litigation and other anti-competitive activities. Perhaps this theory will be applied to patent trolls proven to have asserted weak patents without an adequate infringement investigation.

And, in late 2012, the U.S. Court of Appeals for the Federal Circuit upheld the standing of a direct purchaser of goods protected by a patent to bring an antitrust suit, under the *Walker Process* theory, against a party which obtained the patent through fraud on the Patent Office. *Ritz Camera & Image, LLC v. Sandisk Corporation*, 700 F.3d 503 (Fed. Cir. 2012).

#### THE EIGHTH NO-NO: RESTRICTING A LICENSEE'S USE OF A PRODUCT MADE BY A PATENTED PROCESS

This No-No concerned restrictions on a licensee's use of a product made by a patented process. This No-No requires little analysis, as it appears to be limited to non-price vertical restraints imposed by a patent owner on its customers. The vertical *price* restraints, of course, are another story – and will be discussed in the final chapter in this series.

With respect to non-price vertical restraints, even in the heyday of skepticism over the “monopoly” powers provided to a patent owner, the Supreme Court generally upheld vertical field-of-use restrictions on unpatented products containing patented components. *See, e.g., General Talking Pictures Corp. v. Western Electric Co.*, 305 U.S. 124 (1938).

The Supreme Court has severely diminished the importance of antitrust law in non-price vertical restraints. *See Leegin Creative Leather Products Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007). Thus, under antitrust law, and as specifically called out by the DOJ-FTC Antitrust Guidelines for the licensing of intellectual property, nearly every non-price vertical restraint will be considered pro-competitive, such as customer restrictions, territorial restrictions, or field-of-use restrictions. However, as noted in a prior discussion, patent law may be the more robust doctrine for invalidating post-sale vertical restraints. As noted, in *Quanta Computer Inc. v. LG Electronics Inc.*, 553 U.S. 617 (2008), the Supreme Court noted that, under the first sale doctrine of patent law, patent rights were exhausted after a first sale. And under copyright law, at least one appellate court has ruled that the first sale doctrine does *not* apply to goods that are first published outside the United States. *See John Wiley & Sons, Inc. v. Kirtsaeng*, 654 F.3d 201 (2d Cir. 2011). The Supreme Court heard arguments in this case last fall. Sup. Ct. Dkt. No. 11-697 (argued Oct. 29, 2012).

#### THE NINTH NO-NO: MINIMUM RESALE PRICE PROVISIONS FOR THE LICENSED PRODUCTS

This No-No was for many years perhaps the most controversial under both patent and antitrust law. It concerned whether a patent licensor could fix the resale price of a good covered by a patent.

Let us start first with *antitrust* law on resale price maintenance. For many years, the Supreme Court rule was that resale price maintenance was illegal *per se* – just like horizontal price fixing. *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). While subject to constant economic critique, the *per se* rule was maintained for nearly 60 years. It was first eroded in *State Oil Co. v. Khan*, 522 U.S. 3 (1997), finding that maximum resale price maintenance was governed by the rule of reason and not the *per se* rule. Finally, the *Dr. Miles* rule fell completely in *Leegin Creative Leather Products Inc. v. PSKS Inc.*, 551 U.S. 877 (2007). Today, at least under federal antitrust law, resale price maintenance is subject to the rule of reason. However, various state regimes continue to believe that resale price maintenance is illegal *per se*, a position also taken by various state attorneys general in enforcement actions. And there is renewed interest in Congress in repealing *Leegin* and reinstating the *Dr. Miles* doctrine. Moreover, winning an RPM case under a rule of reason is a real possibility.

However, despite the *per se* prohibition under antitrust law, the Supreme Court had also determined that patent law would prevail – an IP owner could set the resale price of products manufactured under its patents. In *United States v. General Electric Co.*, 272 U.S. 476 (1926), the Court assessed an agreement between General Electric, the manufacturer of light bulbs and owner of the patent covering the manufacture, and its competitor, Westinghouse, licensed to manufacture bulbs under the patents. General Electric set the price that Westinghouse could charge for bulbs manufactured under the patents. While ostensibly a price-fixing cartel, the Court allowed General

Electric, the licensor, to set Westinghouse's prices. Over time, some limits were placed on the *General Electric* rule. For example, in *United States v. Line Material Co.*, 333 U.S. 287 (1948), the Court did not apply *General Electric* when licenses were given to several firms in an industry. See also *United States v. New Wrinkle, Inc.*, 342 U.S. 371 (1952) and *United States v. United States Gypsum Co.*, 340 U.S. 76 (1950). That limitation on *General Electric* was also applied by lower courts, e.g., *Newburgh Moire Co. v. Superior Moire Co.*, 237 F.2d 283 (3rd Cir. 1956) and *Tinnerman Products v. George K. Garrett Company, Inc.*, 185 F.Supp. 151 (E.D. Pa. 1960), *aff'd*, 292 F.2d 137 (3rd Cir. 1961).

The 1995 DOJ-FTC Antitrust Guidelines claimed that *General Electric* had been overruled and opined that fixing a licensee's resale price was *per se* illegal, under the then-prevalent *Dr. Miles* rule. If Congress should determine to reinstate the *per se* rule under *antitrust* law, query what will remain of the *General Electric* doctrine under *patent* law?

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What remains today of the Nine No-Nos? And where are the fault lines in the antitrust and patent tectonic plates? For the most part, all of the Nine No-Nos which pertain to vertical distribution of goods covered by intellectual property are now subject to the rule of reason. As such, a challenge to a patent licensing practice under the antitrust laws will likely only be successful where the patent holder imposing the restraint has monopoly power, or where the vertical restraint is accompanied by horizontal agreements between competitors which adversely impact competition.

But the antitrust laws still do have considerable relevance to current patent law practices. There are at least "Four Frowned-Upons":

1. Generic and branded pharmaceutical patent settlements where the branded pays the generic a "reverse payment" to stay off the market for some period of time. This practice will be examined carefully by the Supreme Court in the *Watson* case. The FTC is proposing a presumptive rule of illegality, or at a minimum some heightened scrutiny.
2. Dedication of standard essential patents ("SEPs") to a standard-setting organization and then failing to honor a commitment to offer fair, reasonable and non-discriminatory ("FRAND") licensing terms and, instead, seeking injunctive relief. This practice was criticized by the FTC in the *Bosch* and *Google* consent decrees, and has been criticized by the Department of Justice in several policy statements and speeches.
3. Creation of a patent pool by horizontal competitors that includes some patents which are not essential to a standard, accompanied by an agreement not to license the non-essential and competitive alternative product patents outside of the pool license. While this practice was not deemed to be patent misuse in the *Princo* case, there remains serious antitrust risk from patent pooling agreements which take competitive technologies off the market.
4. Resale price maintenance agreements in patent licensing. It is not clear whether the patent law doctrine articulated in the *General Electric* case remains valid – we think it has been whittled away to virtually no protection. And while the Supreme Court in *Leegin* has said that resale price maintenance is subject to a rule of reason analysis in federal antitrust cases, that doctrine may not survive legislative reform, subjects the licensor to a robust rule of reason analysis, and is subject to *per se* attack under state law by aggressive private plaintiffs and state attorneys general.

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