Collective Ex Ante Negotiations: Proceed At Your Own Peril

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Introduction

Arguments for Collective Ex Ante Negotiations will:
• Provide certainty for standards implementers regarding input costs for IPR
• Prevent “hold up” and ex post anticompetitive conduct
• Create efficiencies and should be deemed procompetitive and not violations of antitrust laws

Do these arguments justify collective fixing of license terms under the antitrust laws?
Rule of Reason Treatment Is Not a Safe Harbor

• Under the rule of reason, joint conduct is analyzed to determine if it is reasonably necessary to achieve a procompetitive result, and the procompetitive effects outweigh the anticompetitive effects.

  *Nat’l Collegiate Ass’n v. Bd. of Regents of the Univ. of Okla., 468 U.S. 85 (1984)*

• Absent specific evidence, joint ex ante fixing of license terms may not be reasonably necessary to achieve a procompetitive result, and the anticompetitive effects may outweigh the procompetitive effects.

Collusive Fixing of License Terms May Not Be Reasonably Necessary

• No evidence that joint fixing of license terms is necessary in light of alternatives -- *e.g.*, voluntary disclosure of license terms.

• No evidence that joint fixing of license terms is necessary in light of existing practices -- *e.g.*, bilateral disclosure of licensing information by IPR owners to interested licensees.
DOJ Business Review Letters Do Not Provide Comfort

In VITA Letter DOJ cautioned against collusion in fixing license terms

• Concluded that VITA policy should not lead to depression of prices for licenses through joint negotiation because such conduct was prohibited.

• “Any efforts to reduce competition by using the...process as a cover to fix downstream prices...would be a per se violation of section 1 of the Sherman Act, and the Department would not hesitate to condemn such activity.”


DOJ Business Review Letters (cont.)

IEEE Letter expressly did not address joint discussion of license terms.

• “The proposed patent information policy permits voluntary commitments to most restrictive licensing terms, but prohibits discussion of specific licensing terms...Based on your statements, we understand that this prohibition extends to joint negotiations of licensing terms within the standards development meetings. The Department observes in this regard that IEEE’s current policies permit limited discussions of costs related to proposed standards. Such discussion, could, in certain circumstances, rise to the level of joint negotiation of licensing terms. You have not requested, and we are not providing, the Department’s views on joint negotiations that might take place inside or outside such standards development meetings or IEEE sponsored meetings.”

Policies Directing Joint Fixing of License Terms Could Be Unreasonable

• Assertion of patents, even *ex post*, standing alone is not anticompetitive conduct, nor is a royalty rate higher than a licensee desires. This is not “hold up.”

• Even if a patent confers market power, it is not an issue of antitrust concern if the patent owner charges a high or supra-competitive rate. “If a monopoly is lawfully obtained, whether derived from IP rights or otherwise, we do not even object to setting a monopoly price.” Remarks of Ass’t Att. Gen. Pate (June 5, 2005)


Unreasonable Effects (cont.)

• “Even if an intellectual property owner can obtain a royalty rate higher than those of other technology owners, members of the [SDO] that chose the standard are not necessarily being held up. The higher royalty rate may be explained by the superiority of its technology. That is, its peerless technology - developed through ‘superior skill, foresight, and industry’ - may explain the ability to charge a premium.”

  Remarks of FTC Chair Majoras (Sept. 23, 2005), quoting United States v. Alcoa, 148 F.2d 416, 430 (2d Cir. 1945)
"Hold Up" Requires Specific Proof

DOJ identifies required conditions for there to be "hold up"

• Owner of essential patent must assert patent _ex post_ and attempt to impose licensing terms "that SDO members could not reasonably have anticipated"

• It is commercially unreasonable to abandon the standard for an alternative, due to cost of standard setting process or cost of developing products to an alternative standard; and

• "most importantly," "if the other SDO members had anticipated the patent holder’s demands, those SDO members could have chosen a different technology that avoided the patent."

_Remarks of Hill B. Wellford, US DOJ (March 29, 2007)_

Hold Up Proof (cont.)

• "This definition is important because it makes clear that hold up involves the loss of opportunity to pursue a meaningful competitive alternative. Hold up involves a market power that is created by a standard itself, _not_ market power that would have existed regardless of the standard. Hold up... does not exist merely because a group of licensees is upset that a patentee holds the key to an essential technology. Hold up certainly does not exist merely by the fact that a patentee charges a particular rate for its royalty when licensees would prefer a lower rate."

Hold Up Proof (cont.)

- Hold up related to alleged false FRAND commitment addressed by 3d Cir. in Broadcom v. QUALCOMM. To establish actionable anticompetitive conduct, proof must establish "(1) in a consensus-oriented private standard-setting environment, (2) a patent holder’s intentionally false promise to license essential proprietary technology on FRAND terms, (3) coupled with an SDO’s reliance on that promise when including the technology in a standard, and (4) the patent holder’s subsequent breach of that promise."

  Broadcom Corporation v. QUALCOMM Incorporated, No. 06-4292 (3d Cir. Sept. 4, 2007), slip. op. at 24

Hold Up Proof (cont.)

FTC cases require intentional conduct that eliminates opportunity to consider meaningful competitive alternatives.

- Dell - alleged that Dell representative certified in writing that proposal did not infringe patent that issued to Dell a year prior to adoption of standard, with no reason for FTC to believe that such statement was inadvertent, and evidence that association would have implemented a different non-proprietary design if it had been informed of patent by Dell.

- Unocal - Unocal provided material misleading information, amended its patent claims to read on regulation, and then once rule adopted asserted its patents.
Hold Up Proof (cont.)

- Rambus - FTC held that Rambus intentionally (i) made deceptive omissions via its continuing concealment of its patents and patent applications during development of standard, (ii) made outright misrepresentations by giving evasive and misleading responses to questions about its conduct, and (iii) used information gained through its participation in the SDO to shape a patent-filing strategy that included filing patent applications covering key parts of the standard being developed.

Collective License Negotiations Could Result In Anticompetitive Buyer Cartel

- Potential licensees of essential IPR typically outnumber potential licensors of essential IPR in connection with a standard, and collusion among licensees to fix license terms could result in the exercise of oligopsonistic market power.

- “Market power also encompasses the ability of a single buyer ("a monopsonist"), a coordinating group of buyers, or a single buyer, not a monopsonist, to depress the price paid for a product to a level that is below the competitive price and thereby depress output. The exercise of market power by buyers ("monopsony power") has adverse effect comparable to those associated with the exercise of market power by sellers.”

DOJ/FTC Horizontal Merger Guidelines, issued April 2, 1992, revised April 8, 1997
Buyer Cartel Effects

- The anticompetitive effects resulting from a buyers’ cartel, including in connection with a cartel of IPR licensees, is that such collusive conduct can “create or increase market power...or facilitate its exercise by increasing the ability or incentive to drive [down] the price of the purchased product, and thereby depress output, below what likely would prevail in the absence of the relevant agreement.”
  
  DOJ/FTC Antitrust Guidelines for Collaboration Among Competitors, April 2000

- See also Sony Electronics v. Soundview Tech., 157 F. Supp. 2d 180, 185 (D. Conn. 2001) (motion to dismiss complaint denied where “[t]he all-or-nothing price set by these colluding purchasers can depress the price below the optimal price that would obtain if usual market forces of supply and demand were at work. The price to consumers does not decrease, but there may be social welfare consequences in the long run, because suppliers will leave the industry (or as Soundview has it, will cease to innovate and invent”).

Buyer Cartel Effects (cont.)

Collusive fixing of license terms for essential IPR may (but not necessarily) enhance static efficiencies by lowering costs, but will harm consumer welfare by decreasing dynamic efficiencies.

- “[T]here are two types of efficiency: static and dynamic. Static efficiency occurs when firms compete within an existing technology to streamline their methods, cut costs, and drive the price of a product embodying that technology down to something close to the cost of unit production. Static efficiency is a powerful force for increasing consumer welfare, but an even greater drive of consumer welfare is dynamic efficiency, which results from entirely new ways of doing business. Economists now recognize that the gains from dynamic efficiency,..., can far outstrip the gains from incremental static improvements.”
Buyer Cartel Effects (cont.)

“Intellectual property laws are aimed at encouraging dynamic efficiency. The same forces that yield the benefits of static efficiency - conditions that encourage rivals quickly to adopt a new business method and drive their production toward marginal cost - can discourage innovation (and thus dynamic efficiency) if the drive toward marginal cost occurs at such an early stage that it prevents recoupment of development expenditures, and makes innovation uneconomical. IP laws, therefore, create rights to exclude, which allow producers to recoup their costs and make the kind of profit that encourages them to engage in inventive-creative behavior.”


- As a result: (i) less innovation could occur; (ii) output of innovative technology would be diminished; and (iii) consumers of standardized products would be denied benefits of superior, more efficient technical solutions.

Conclusion

- Collective negotiation of license terms in a standards body may, depending on specific facts, result in efficiency enhancing effects.

- Significant potential for anticompetitive effects that harm consumer welfare exist, counseling against the adoption of across-the-board policies for ex ante joint determination of licensing terms.
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