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Avoiding the Antitrust Traps in Licensing Intellectual Property

March 30, 2010

A Mayer Brown Webinar

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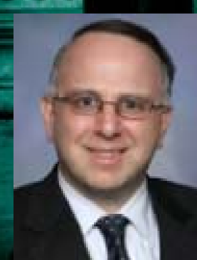

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Introduction

- Historical View: Intellectual property law and antitrust law inherently conflict because intellectual property laws create monopolies.
- Current View: Intellectual property and antitrust are complementary in encouraging innovation, industry, and competition.
- US and EU antitrust agencies recognize the need for IP licensing, where appropriate
  - Fact-specific, economically rigorous analytical approach
    - "[A]ntitrust concerns may arise when a licensing arrangement harms competition among entities that would have been actual or likely potential competitors . . . **in the absence of the license**." (IP Guidelines)
    - In the EU: "[Technology Transfer Agreements] will usually improve economic efficiency and be pro-competitive as they can reduce duplication of research and development, strengthen the incentive for initial research, spur incremental innovation, facilitate diffusion and generate product market competition." (Recital 5, Technology Transfer Block Exemption)

Avoiding the Antitrust Traps

THE GENERAL FRAMEWORK

The Legal Framework in the United States

- Sources of competition regulation
  - Sherman Act and federal law
  - Case law
  - Agency Guidance (IP Guidelines)
- Mode of analysis
  - Per se offenses
  - Rule of reason analysis

The Legal Framework in the European Union

- Articles 101(1), 101(3) and 102 of the Treaty on the Functioning of the European Union ("TFEU")
- Block Exemptions
- European Commission Guidelines on the TTBE ("TTBE Guidelines")
  - Commission Decision 2004/C 101/02
- Relevant case law
- Applicable Member State rules

The Basic Antitrust Analysis in the EU: Hardcore Restrictions

- Hardcore restrictions – EU equivalent to the Per Se Rule?
- Price Fixing
- Agreements with Competitors
  - Limiting output
  - Market or customer sharing
  - Restrictions on the Licensee's use of its own technology
- Agreements with Non-Competitors
  - Passive sales

The Basic Antitrust Analysis in the EU: Rule of Reason

- Rule of Reason Analysis: TTBE
- The EU will assess whether an exemption applies under the TTBE – this is a prescriptive test.
- Where the TTBE does not apply, the EU will ask:
  - Does the license agreement restrict actual or potential competition that would have existed without the contemplated agreement. If so, then it will be caught by Article 101(1).
  - Does the license agreement restrict actual or potential competition that would have existed in the absence of the contractual restraint. If so, then it will be caught by Article 101(1).

Avoiding the Antitrust Traps: US Safety Zones

- The licensor and its licensees collectively account for no more than 20% of each relevant "goods market"
- There are four or more additional independently controlled technologies in the "technology market"
- There are four or more independently controlled entities in the "innovation market"
- (IP Guidelines, § 4.3)

Avoiding the Antitrust Traps: EU Block Exemptions - Safety Zones

- Trade mark, software and copyright licensing agreements, creating a safe harbor for technology licensing agreements restrictions, on the following conditions:
  - Subject of license is patent, design right or know-how, plus
  - License is between two parties who can be competitors
  - Market share thresholds are not exceeded:
    - For non-competitors, the market share of each party to the agreement does not exceed 30% of relevant product/technology market
    - For competitors, combined market share does not exceed 20% of the relevant product or technological market
- Trade mark and copyright licences if: (i) ancillary licences – do not constitute the primary object of the agreement, (ii) necessary to exploit the licensed technology, and (iii) software copyright licences - only for the purpose of producing copies for resale

Avoiding the Antitrust Traps: EU Block Exemptions - Safety Zones

- Permitted licence obligations include (TTBE Guideline 155):
  - Confidentiality obligations
  - Obligations on licensees not to sub-license
  - Obligations not to use the licensed technology after the expiry of the agreement, provided that the licensed technology remains valid and in force
  - Obligations to assist the licensor in enforcing the licensed intellectual property rights
  - Obligations to pay minimum royalties or to produce a minimum quantity of products incorporating the licensed technology
  - Obligations to use the licensor’s trade mark or indicate the name of the licensor on the product

Avoiding the Antitrust Traps: EU Block Exemptions – Outside the Safety Zones

- Technology pools
- Lapsed IP rights – but "know-how" may fall within
- Hardcore restrictions
- Excluded restrictions fall outside the TTBE and are assessed individually:
  - Exclusive grant back obligations
  - Exclusive assignment back obligations
  - No challenge clauses: EU is of the view that invalid Intellectual Property Rights stifle innovation and should be eliminated
  - Exploitation/development by the licensee of its own technology if non-competing

Avoiding the Antitrust Traps

AVOIDING THE SPECIFIC TRAPS

Specific Traps – A Summary

- Price restrictions
- Territorial restrictions
- Field of Use restrictions
- Customer restrictions
- Tying/Bundling arrangements
- Exclusive licensing
- Refusal to license
- Patent pools
- Royalty provisions

Avoiding the Antitrust Traps: Price Restrictions (US)

- In the U.S., a licensor can set the price of the first sale of a patented product if the intellectual property and patented product cover the same space. *United States v. Gen. Elec. Co.*, 272 U.S. 476, 478–79 (1926).
  - DOJ and FTC had condemned this practice as unlawful "per se" resale price maintenance. United States Department of Justice-Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property*, § 5.2 (1995).
  - The Supreme Court recently confirmed that resale price maintenance is judged under the rule of reason. *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 127 S.Ct. 2705 (2007).
- There are limits . . .

Avoiding the Antitrust Traps: Price Restrictions (US)

- Limitations on the *GE* rule:
  - The GE Rule will not apply outside the “paradigm case.”
    - Product requiring multiple patents to make?
  - Generally not applicable in pooling arrangements. *United States v. Line Material Co.*, 333 U.S. 287, 304 (1948)
  - Horizontal agreements on price restraints among either licensees or patentees with respect to multiple licenses on one patent. *See United States v. U.S. Gypsum Co.*, 333 U.S. 364, 371 (1948).
  - A price restriction on goods that are made with technology on goods other than the licensed technology. *Cummer-Graham Co. v. Straight Side Basket Corp.*, 142 F.2d 646, 647 (5^{th} Cir. 1944).
- Price restrictions, even if legal, may raise questions.

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Avoiding the Antitrust Traps: Price Restrictions (EU)

- Hardcore Restrictions apply
- Under EU law, a technology license with a minimum price restriction will be deemed anticompetitive and subject to challenge under relevant competition laws. (TTBE Article 4(1)(a) and Guidelines 79-80 and 97)
- EU Law prohibits licenses from specifying the following with regard to products made from the licensed technology:
  - the exact price to be charged;
  - a minimum/maximum/recommended price;
  - a price list with allowed maximum rebates; and
  - any disincentive to deviate from agreed pricing levels (e.g., an increase in royalties paid following a reduction in price).

Avoiding the Antitrust Traps: Territorial Restrictions (US)

- Patent Licenses: A patentee may license (or refuse to license) any right under his patent to the whole or any specified part of the United States. Patent Code, § 261.
- However, a territorial restriction in a patent license could be illegal if:
  - (a) It is a restriction on resale subsequent to the first authorized sale of the patented product (the "exhaustion doctrine").
  - (b) The license is simply a pretext for a horizontal market division scheme.

Avoiding the Antitrust Traps: Territorial Restrictions (US)

- Copyright Licenses: A copyright owner may license his copyright "whether or not … limited in time or place of effect."
  - Copyright Act of 1976, § 101.
  - However, such a territorial restriction is subject to a rule of reason analysis.
- Trade Secret Licenses: The owner of a trade secret or know-how may license its use "with restrictions as to territory."
- Trademark Licenses: A territorial restriction in a vertical trademark licensing arrangement will be subject to a rule of reason analysis.

Avoiding the Antitrust Traps: Territorial Restrictions (EU)

- General rule: a hardcore restriction under TTBE:
  - Competitors are prohibited from agreeing not to produce in certain territories, or not to sell actively or passively in certain markets
  - Non-competitors prohibited from passive sales restrictions, but subject to a number of exceptions
- Applies in cases where the licensee is still free to use its own technology
- There are certain exceptions, e.g., in relation to field of use, set out in the TTBE Guidance 88-93. See also Case C-258/78 *Nungesser v. Commission* [1982] ECR 2015.
- Selected exceptions:
  - *de minimis* market share of threshold of 30% (TTBE Guideline 100)
  - limited 2-year exclusivity rights in order to establish a market for the licensed product (TTBE Guideline 101).

Avoiding the Antitrust Traps: Field of Use Restriction (US)

- Patent Licenses: A patentee may lawfully restrict a patent license to a particular field of use.
- Field of restrictions going beyond products made under the patent are questionable.
- Field of use restrictions for unpatented products manufactured through a patented process are subject to rule of reason analysis.
- Copyright, Trade Secret Licenses and Trademark Licenses: Same.

Avoiding the Antitrust Traps: Field of Use Restriction (EU)

- All licenses: Field of use restrictions allowed subject to certain conditions
  - Restriction should not cause licensee to cease to be a competitive force outside of the licensed field of use.
  - No underlying market share agreement.
- Captive use restrictions limitations
  - Where the licensor is a supplier of components, captive use restrictions will normally qualify for an exemption. Need to be able to objectively justify.
- The analysis of customer restrictions in patent, copyright, trade secret and trademark licenses is generally analogous to the analysis of field of use restrictions in patent licenses.

Avoiding the Antitrust Traps: Customer Restrictions (EU)

- Customer allocation is a hardcore restriction
- Certain exceptions in non-reciprocal agreements:
  - Both the licensor and licensee may be restrained from making passive or active sales to a customer group reserved exclusively for the other party (TTBE Article 4(1)(c)(iv))
  - Licensee may be restrained from making sales to another licensee provided that the protected licensee was not a competitor of the licensor at the time of the conclusion of the license
  - Licensee may be required to produce licensed products for a particular customer as an alternative supplier to that customer
  - Captive use restrictions may apply

Avoiding the Antitrust Traps: Tying and Bundling (US)

- Patent Licenses: A “tying” arrangement in a patent license is illegal if:
  - The tied product/service is separate from the patent to be licensed.
  - An actual “tie” exists between the tying patent and the tied product/service.
  - The arrangement affects a “not insubstantial” amount of interstate commerce in the tied product/service.
  - The party imposing the tie has sufficient economic power in the market.
- Under the patent misuse doctrine, a patent is not presumed to convey economic power.
- Courts may use the rule of reason to analyze tying arrangements.
- Copyright Licenses, Trade Secret Licenses, and Trademark Licenses are substantially analogous to patent licenses.

Avoiding the Antitrust Traps: Package Licensing (US)

- Patent Licenses: A single patent license may lawfully grant the licensee rights under multiple patents (a “package license”).
- A package license may be illegal if the patent owner’s grant of a particular desired patent is “tied to” or “conditioned upon” the licensee’s acceptance of an undesired broader package license.
- Copyright Licenses, Trade Secret Licenses, and Trademark Licenses are substantially analogous to the analysis of package licensing of patents.

Avoiding the Antitrust Traps: Tying and Bundling (EU)

- The Commission acknowledges that tying and bundling may have no anti-competitive consequences and is prepared to accept efficiency arguments and examine market-specific conditions
- Market may be provided with:
  - Better products or offerings in cost-effective ways.
  - Significant savings in production, distribution and transaction costs and to improved quality.
  - Fundamental part of many economic activities.
- The Commission will normally take action only where:
  - An undertaking is dominant in the tying market;
  - The tying and tied products are distinct products (such that, in the absence of bundling, a substantial number of customers would purchase them separately); and
  - The tying practice is likely to lead to anti-competitive foreclosure

Avoiding the Antitrust Traps: Tying and Bundling (EU)

- European Commission recognises that tying can give rise to efficiency gains and be exempt.
- Foreclosure effect of tying and bundling where licensor has a significant degree of market power in the tying product (e.g., *IBM*, *Microsoft*).
- Where tying acts as an abuse of a dominant position, the EU will act.
- Tying and bundling is explicitly listed as an abuse under Article 102 of the TFEU (see also Case C-53/92P*Hilti AG v Commission* [1994] ECR I-667 and Case T-30/89 *EurofixBanco v Hilti AG* [1991] ECR II-1439).

Avoiding the Antitrust Traps: Tying and Bundling (EU)

- In *IBM* (*OJ 1984 L118/24*), the Commission objected to IBM's practice of only selling CPUs with memory included, in a practice known as "memory bundling". This, together with other abusive practices, foreclosed the market. IBM undertook to amend its practices in return for the Commission suspending proceedings under Article 102.
- In Case COMP/C-3/37.792 *Microsoft/W2000*, the Commission set down the test for tying. In order for a breach of Article 102 to occur, the following was required:
  - The tying and tied goods had to be two separate products
  - The tying undertaking had to be dominant in the product and technological markets
  - Customers could have no choice in obtaining the tying product without the tied product
  - The tying had to foreclose competition in the relevant market

Avoiding the Antitrust Traps: Exclusive Licensing (US)

- Generally, an intellectual property owner may lawfully "grant one or more exclusive licenses which restrict the right of the licensor to license others and possibly also to use the technology itself." (IP Guidelines, § 4.1.2; 35 U.S.C. § 261)
- Grant of an exclusive license may be reportable under the Hart-Scott-RodinoAct.
  - Both apply to purchase of assets, including patents and other IP, as well as purchasing an exclusive license to a patent or other IP

Avoiding the Antitrust Traps: Exclusive Dealing (US)

- Exclusive Dealing: prevent or restrict licensee from using, selling, licensing, competitors' technologies
- Evaluated under the rule of reason. Agencies consider:
  - Foreclosure
  - Duration
  - Concentration
  - Barriers to Entry
  - The responsiveness of supply and demand to changes in price
  - Pro-competitive justifications
- An exclusive dealing arrangement could be illegal if it restricts the licensee from dealing in non-infringing competing products.

Avoiding the Antitrust Traps: Exclusive Licensing (EU)

- TTBE Guideline 165:
  - most exclusive agreements between non-competitors will be excluded or benefit from exception
- Exceptions:
  - where the licensor has significant degree of market power
- Considerations:
  - competitive significance of licensor
  - market strength of licensor and resources to exploit the product in the licensee's territory
- Assess impact on competition caused by the exclusive license.

Avoiding the Antitrust Traps: Refusal to Licence (US)

- Unilateral refusals to license at least presumptively do not violate antitrust law.
- Some courts have created a rebuttable presumption that refusal to license a copyright is a valid business justification. Plaintiff can overcome this presumption with evidence that the monopoly created by refusal to license was unlawfully acquired.
- Evidence of pretext may rebut the presumption that refusal to license a patent is a valid business justification.
  - *SeeImage Technical Services, Inc. v. Eastman Kodak Co*., 125 F.3d 1995 (9th Cir. 1997).
- Other courts say subjective intent of patent holder's refusal is irrelevant, and refusal to license is per se legal.
  - *See In re Independent Service Organizations Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000), *cert. denied*, 531 U.S. 1143 (2001).

Avoiding the Antitrust Traps: Refusal to Licence (EU)

- Breach of EU prohibition on abuse of dominance in "exceptional circumstances" if:
  - IP is indispensable for entering a related market;
  - refusal is likely to have negative effects on competition in that market; and
  - refusal is not objectively justified (joined Cases C-241/91 and C242.91P *Magill* [1995] ECR 743; see also Case 238/87 *Volvo/Veng*[1988] ECR 6211)
- EU draws a distinction between downstream and upstream markets to establish the "exceptional circumstances" (Case C-418/01 *IMS Health Inc. v. Commission*). See also Case T-201/04 *Microsoft v. Commission* [2007] 5 CMLR 846, which concerned upstream markets.
- Defense: objective justification
- Collective boycotts

Avoiding the Antitrust Traps: Patent Pools (US)

- Key questions: Are the rights you're licensing jointly complements or substitutes?
- Competitors with complementary or blocking IP can cross-license or pool their IP as long as there is a pro-competitive justification
  - Full exploitation
  - Remove blocking patents
  - Reduce transaction costs
  - Avoiding infringement litigation
- Reasonableness used to determine if IP is complementary or blocking

Avoiding the Antitrust Traps: Patent Pools (EU)

- Two or more parties assemble a package of technology licensed to contributors to the pool and 3rd parties
- Agreements establishing patent pools not covered by TTBE, but individual licences granted from pool to 3rd parties are treated like all other licence agreements
- Can be pro-competitive (reduce transaction costs, one-stop licensing)
- Competitive risk depends on type of technology
  - **Substitute technologies** - likely breach of Article 101(1) and no exemption
  - **Complementary technologies** – usually falls outside scope of Article 101(1)
  - **Essential technologies** - usually falls outside scope of Article 101(1)
  - **Non-essential technologies** – can amount to collective bundling
- Commission Guidelines – main principles for assessing competition restrictions:
  - Examine market position of the pools
  - Pools should not unduly foreclose 3rd party technologies or limit the creation of alternative pools — licensors and licensees must be free to develop competing products and free to grant/obtain licenses outside the pool
  - Grant-back obligations should be non-exclusive and limited to developments important to use of pooled technology

Avoiding the Antitrust Traps: Royalties (US)

- No limit on the amount that can be charged.
- Patent holders may exact "pre-issue" patent royalties and may license know-how even if nothing is patented.
- The patentee's use of a royalty agreement that projects beyond the expiration date of the patent is generally illegal.
- Some limited exceptions:
  - Deferred payment instead of a post-expiration royalty.
  - A package license which terminates when the final patent in the package expires.
  - The royalty is based on the licensee's total sales of particular products.

Avoiding the Antitrust Traps: Royalties (EU)

- Royalties can originate from a jurisdiction without any patents if there are pending patent applications or the license includes essential, non-patented IP (trade secrets) or other IP, such as trademarks.
- Royalty should be tied to the trade secret's value and should not be a means of excessively pricing for a license. Excessive pricing may be seen as an abuse of a dominant position under Article 102. See Case 402/85 *Basset v. SACEM*[1987] ECR 1747 and Case 395/87 *Ministère Public v Jean-Louis Tournier* [1989] ECR 2521).
- Royalty should be expressly linked to the IP and reflect its actual value. The Commission will carefully consider if excess royalties are being charged (see *Microsoft/W2000*).

Avoiding the Antitrust Traps

CONCLUSION

Similarities Between US and EU Position

- Both examine economic effects
- Neither presumes that IP = market power
- Both provide safe harbors
- Per se violations:
  - Certain Output Restraints
  - Horizontal Market Allocations
- Rule of reason/objective justifications for the rest

Distinctions Between US and EU Position

- EU: assesses “objective necessity” of individual license provisions
- EU: more concerned with intra-brand competition and hence vertical restraints
- Because of Common Market, EU prohibits most territorial restrictions on passive sales
  - “Passive sales” are sales made in response to an unsolicited request and not the result of presence in territory
- EU: minimum resale price fixing illegal, not Rule of Reason
- Refusal to grant a license in EU can be abusive under “exceptional circumstances”:
  - No objective justification
  - IP is indispensable
  - Other party intended to produce new goods distinct from IP owner’s goods
  - Potential customer demand for new goods
- Bottom line: If refusal to license blocks a new and innovative product, it may be abusive

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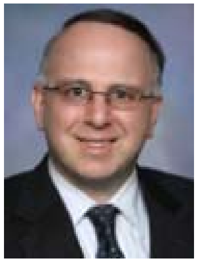

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Questions & Answers

Thank you