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TO: Department of Justice, Antitrust Division; Federal Trade Commission (ATR.LPS-PAEPublicComments@usdoj.gov)
FROM: Richard Wolfram
DATE: April 5, 2013
RE: Response to Request for Public Comments On DOJ-FTC Hearing on Patent Assertion Entities

At the December 2012 Department of Justice-Federal Trade Commission Hearing on patent assertion entities (PAEs) and in response to the Request for Public Comments, participants and other commentators have amply and authoritatively described and assessed the impact of PAEs on innovation and competition, both positive and negative.

I am submitting this comment, in my personal capacity and drawing from my own experience, for one limited purpose – to address the viability of a Sherman Act Section 2 monopolization claim against a PAE which has repudiated the commitment of its predecessor (direct or indirect), which participated in a standard setting organization (SSO), to license any of its intellectual property "essential" to a standard developed by that SSO on fair, reasonable and non-discriminatory (F/RAND) terms.[1]

In a recent speech Deputy Assistant Attorney General Renata Hesse discussed the question of Section 2 antitrust liability for patent hold-up by owners of standard essential patents (SEPs), wherein they make knowingly false F/RAND commitments to the SSOs in which they participate and which then, in reliance on such commitments, develop standards incorporating their SEPs, resulting in industry lock-in.[2] She further noted that the question has been raised whether Section 2 liability for such conduct, if any such liability obtains, should be limited as a matter of law and policy "exclusively to instances in which the patent holder intentionally deceived the SSO while it designed the standard." For instance, in contrast to the facts in *Broadcom v. Qualcomm*[3], in which Qualcomm was found to have intentionally deceived the SSO at the time it made its F/RAND commitment, one can imagine a scenario in which an SSO participant holding an SEP

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[1] This comment assumes for purposes of this discussion that the ever-thorny question of what constitutes a breach of a F/RAND commitment can be resolved and that a determination of breach can be made in a given case.

[2] "IP, Antitrust and Looking Back on the Last Four Years," Deputy Attorney General Renata Hesse (Feb. 8, 2013), *available at* http://www.justice.gov/atr/public/speeches/292573.pdf.

[3] *Broadcom Corp. v. Qualcomm Inc.*, 501 F.3d 297 (3d Cir. 2007).

makes a F/RAND commitment in good faith and then subsequently changes course and violates its F/RAND commitment after the standard is set. It has been argued, Ms. Hesse notes, that in such circumstances "the competitive process may be equally disrupted if there were alternatives that the SSO would have included but were ultimately excluded because of the patent holder's F/RAND commitment." As Ms. Hesse explicitly encouraged members of the bar to address this question, I write in response to this request, but now specifically with respect to the scenario in which the entity repudiating the F/RAND commitment is not the original obligor but its (direct or indirect) assignee, a PAE, as such conduct also squarely falls within the scope of the FTC/DOJ workshop on PAEs.

Some five years ago I co-authored with David Balto a public Request for Investigation submitted to the FTC by the American Antitrust Institute alleging patent hold-up by Rembrandt, Inc, a PAE (referred to therein more broadly as a "non-practicing entity"), with respect to technology critical for the transmission of digital television signals, which was central to the nationwide conversion to digital TV.[4] In that Request (the "petition") we explained the basis for possible claims under Section 5 of the FTC Act and, notably for present purposes, also Section 2 of the Sherman Act, for patent hold-up by Rembrandt with respect to a F/RAND commitment made by its (indirect) predecessor, AT&T, to an SSO responsible for developing standards for digital television.

I incorporate the AAI's petition herein by reference, first, in order to offer a concrete set of facts and allegations that may serve as a more meaningful basis for readers to examine the viability of a Section 2 claim against a PAE. I emphasize, however, that I am not seeking in any way to revive the claims therein.[5] Instead, the petition is offered here, and serves in part as the basis for this comment, only by way of example. Rather than repeat the allegations of the petition, this comment assumes familiarity by the reader with it and elaborates on the legal basis for the viability of a Section 2 claim aimed at patent hold-up by a PAE, using the allegations in the petition as one example.

Before proceeding further with this analysis, it is worth pausing for a moment to explain why it might be useful to be able to apply Section 2 to patent hold-up by PAEs if Section 5 of the FTC Act might be sufficiently flexible and robust to address the same conduct. The answer, of course, is that Section 5 enforcement is limited to the FTC; Section 5 enforcement (based on a theory of unfair competition and/or unfair acts or practices rather than on Section 2 alone) has been subject to criticism for a perceived lack of limiting principles (a view on which I express no opinion here); and Section 2 is more clearly developed in the law, generally viewed as being more rigorous, and enables the

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4 Request for Investigation of Rembrandt, Inc. for Anticompetitive Conduct That Threatens Digital Television Conversion, Petition to the Federal Trade Commission by the American Antitrust Institute, Bert Foer (March 26, 2008), *available at* http://www.antitrustinstitute.org/files/AAI%20FTC%20Petition%20Rembrandt%203.26.08_040120081130.pdf

5 The underlying facts were the subject of long-running litigation, in substantial part addressing the prior question of whether the standard(s) at issue even read on the relevant IP.

DOJ, state enforcers and private entities to seek injunctive relief and treble damages. In other words, if Section 2 applies to patent hold-up by PAEs, such conduct is subject to a substantially wider array of potential enforcement options and remedies than under Section 5, thereby providing a stronger deterrent effect.

Finally, this comment does not purport to offer a full 'white-paper' treatment of the question under review but instead only to suggest the outlines of the argument for continuing analysis.

1. Repudiation of a F/RAND commitment is exclusionary conduct under Section 2 and distinct from exploitation of (legitimate) monopoly power.

Repudiation of a F/RAND commitment, either by the original obligor to the SSO or its direct – or a subsequent – assignee, of the intellectual property rights in question, can constitute exclusionary conduct within the meaning of Sect. 2, no less than deception by the obligor on that commitment, as explained below.

Assignee succeeds to F/RAND commitment. First, many SSOs today, cognizant of the possibility of patent hold-up by PAEs, are making explicit in their governing rules that any assignee of SEPs subject to a F/RAND commitment takes such IP subject to that F/RAND commitment. Over and beyond any such undertakings by SSOs, however, it is clear as a matter of law that an assignee succeeds to an obligor's licensing rights and obligations (including F/RAND constraints).[6] This principle is a necessary predicate to any claim of Section 2 liability of a PAE for patent hold-up.

Standard setting may provide the occasion for various forms of opportunism. Second, it is well established that standard setting bodies may provide the occasion for opportunistic conduct. The Commission's enforcement actions in *Dell Computer* and *Unocal*, its allegations in *Rambus*, and the *Broadcom v. Qualcomm* suit, among others, offer examples. The forms of opportunism are myriad, like the forms of exclusionary conduct. As the Supreme Court has observed, standard setting presents many opportunities for exclusionary conduct. *See Am. Soc'y of Mech. Eng'rs v. Hydrolevel Corp.*, 456 U.S. 556, 571 (1982) ("a standard-setting organization . . . can be rife with opportunities for anticompetitive activity"). Firms can secure monopoly power by failing

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[6] *See, e.g., Moldo v. Matsco, Inc. (In re Cybermetic Servs.)*, 252 F.3d 1039 (9th Cir. 2001), *cert. denied*, 2002 U.S. LEXIS 683 (2002) (citing *Keyston Type Foundry v. Fastpress Co.*, 272 F. 242, 245 (2d Cir. 1921) ("It had long passed into the textbooks that . . . an assignee acquired title subject to prior licenses of which the assignee must inform himself as best he can at his own risk")); *Worley v. Tobacco Co.*, 104 U.S. 340, 344 (1881) ("The assignee of a patent-right takes it subject to the legal consequences of the previous acts of the patentee."); *Medtronic AVE Inc. v. Advanced Cardiovascular Sys. Inc.*, 247 F.3d 44, 60 (3d Cir. 2001) ("an assignee obtains only the right, title and interests of his assignor at the time of his assignment, no more"); *see also* Alice Haemmerli, "Why Doctrine Matters: Patent and Copyright Licensing and the Meaning of Ownership in Federal Context," 30 Columb. J.L & Arts 1, n.247 (Fall 2006) (noting that patents are taken subject to existing licenses); and *see generally* 35 U.S.C. § 261 ("Subject to the provisions of 35 U.S.C. §§ et seq. [the Patent Code], patents shall have the attributes of personal property.").

properly to disclose intellectual property rights, or by failing to abide by an obligation to license on a reasonable and non-discriminatory basis.

The key is whether the conduct distorted competition for the standard. Third, any form of conduct – deception or otherwise – that subverts the proper ends of a standard setting collaboration, by distorting competition for the standard and harming consumer welfare, can be "exclusionary" within the meaning of Sect. 2. When a promise to do a future act is later repudiated or breached, whether by the original promisor itself or by a subsequent assignee, and that repudiation or breach cannot be excused by accident or other legal justified cause, but instead results from bad faith, it is immaterial whether the intent not to honor the commitment is formed only after it is originally made. The potential anticompetitive consequences are no different from those in the more conventional scenario of a contemporaneous intent to deceive at the time of making the commitment (e.g., as alleged in *Rambus*, *Qualcomm*): the reliance triggered by the giving of the commitment, and the expectation that the commitment will be fulfilled, which were a critical basis for the SSO's selection of the standard in question (where the SSO participants understood that it may encompass the obligor's IP rights), are undermined and competition for the standard has been distorted because the evaluation of the relative merits of alternative technologies, which includes the cost of licensing as a significant factor, has itself been distorted.

The Supreme Court has long held that anticompetitive manipulation of a standard setting process to protect or obtain market power may violate the Sherman Act. *See Hydrolevel*, *Allied Tube*. One of the key lessons from *Allied Tube* is that the predicate exclusionary conduct in standard setting is not limited to deception – and may even literally comport with an SSO's rules – because opportunistic conduct that subverts the standard setting process and harms competition can take various forms. For instance, the vote-packing conduct in *Allied Tube* itself was not deceptive – the defendant steel company and its allies openly recruited new voters for the vote on the insulation standard – but the Second Circuit and the Supreme Court upheld the jury's verdict that the defendant "subvert[ed] the consensus standard-making process" and thus violated the Sherman Act.

In the case of the Advanced Television Systems Committee (ASTC), for instance – the SSO that selected for the standard IP ultimately assigned to Rembrandt – the F/RAND commitment, like F/RAND commitments to virtually any other SSO, was intended to constrain the acquisition and exercise of monopoly power by participants in the ATSC with respect to their IP that might have been encompassed by the digital standard. Rembrandt allegedly repudiated the ATSC F/RAND commitment, first by refusing to license its relevant technology on F/RAND terms to manufacturers pursuant to its obligation to the ATSC, in demanding non-F/RAND royalties from the networks and cable companies, and then by suing them for infringement. By this repudiation, Rembrandt both acquired and exercised monopoly power. This conduct is exclusionary in that the repudiation of the F/RAND commitment originally made by AT&T effectively undermined the reliance of the other SSO members on that commitment, which was the basis for their selection of AT&T's IP for the standard – not of course in the present sense of undermining their reliance at the time of the selection process, but in the sense of *post facto* distorting competition for the standard because had they known the commitment would be repudiated, they would not have chosen that IP for the standard provided alternatives existed, or arguably even if no alternatives existed, in which case they might have selected no standard at all. Thus, the SSO members excluded alternative technologies in the competition for the standard as a result of their reliance on the commitment that the F/RAND obligation would be fulfilled in selecting AT&T's IP for the standard. More specifically, they relied on the assurance of F/RAND pricing in their determination of the appropriate standard for digital transmission technology and the proprietary technology (including AT&T's) that may be deemed to be encompassed by it.

Repudiation by a PAE of a F/RAND commitment is opportunistic and a form of 'cheap exclusion'. The petition characterized Rembrandt's conduct both as opportunistic and as a form of 'cheap exclusion' – two characterizations that apply broadly to a variety of conduct that has been found to violate Sect. 2 in other cases. First, with relevance to standard setting, former DOJ chief economist Carl Shapiro has explained that "a firm might obtain a dominant position based in part on certain 'open' policies that induce reliance by complementary firms, and then later exploit that position by offering less favorable interconnection terms or by refusing to interconnect with them altogether."[7] And "[w]hen the effects of opportunism are market-wide," he added, "antitrust concerns arise."[8]

Further, as former FTC Competition Bureau Director Susan Creighton and co-authors explain, "opportunistic behavior occurs when a party to a relationship (like a contract) engages in the relationship, where the behavior is contrary to the other parties' legitimate expectations but not necessarily to the precise rules governing the arrangement. Such behavior generates no efficiency benefits, and not only transfers wealth but also raises transactions costs by compelling wasteful investments in protecting against future opportunism. It is, in short, inefficient on its face. Because such behavior is inefficient even if it does not produce market power after the facts, it can have no claim to legitimacy under an antitrust regime."[9] A PAE's repudiation of a F/RAND commitment – and as alleged in the petition regarding Rembrandt – likely has market-wide effects and transfers wealth without commensurate efficiency benefits.[10]

Second, opportunistic behavior that confers market power is a potential form of 'cheap exclusion'. Conduct that qualifies as cheap exclusion is marked by little or no cost to the actor engaging in the conduct and an absence of cognizable efficiencies. The conduct of a PAE that engages in patent hold-up, as alleged in the petition on the part of

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[7] Carl Shapiro, Exclusionary Conduct 15 (Testimony Before the Antitrust Modernization Commission, Sept. 29, 2005), available at http://faculty haas.berkeley.edu/shapiro/amexclusion.pdf.

[8] *Id.* at 16.

[9] S. Creighton, D. Bruce Hoffman, T. Krattenmaker, E. Nagata, "Cheap Exclusion," 72 Antitrust L. J. 975, 987-88 (2005).

[10] A PAE (and more generally, an NPE) can of course achieve efficiencies by introducing intellectual property rights into the stream of commerce. But such efficiencies can be achieved without a PAE's repudiation of its F/RAND obligation, and the attendant anticompetitive effects, which effectively negate any such possible efficiencies.

Rembrandt, qualifies on both accounts. As Creighton *et al.* note, opportunism in standard setting is a good example of cheap exclusion and its key features can be found in such cases as *Allied Tube*, *Hydrolevel* and *Rambus*: "First, in each of those cases, the alleged conduct did not create wealth but simply transferred it, and so had no possible claim to efficiency. Second, the conduct was cheap (in some cases, almost costless) to the firm engaging in it. Third, the returns from successfully transforming the exclusionary conduct into monopoly profits were large in proportion to the costs of trying. [. . .] [And, f]inally, the cheap exploitation of opportunism occurred where a handy source of durable market power already existed." [11] Thus, for instance, in *Allied Tube*, *Hydrolevel*, *Unocal*, *Dell*, *Broadcom v. Qualcomm*, and as alleged in *Rambus*, among other cases, the standard setting organization had the power to confer market power by choosing one party's processes or by excluding another's, resulting in the potential infliction of harm to consumer welfare.[12]

Repudiation of F/RAND commitment is similar to other opportunistic conduct held to be the basis for stating a claim of exclusionary conduct under Section 2. As former Bureau of Competition Deputy Director Sean Royall explained in an article several years ago, repudiation of a F/RAND commitment to an SSO is similar to other conduct that has been held to constitute exclusionary conduct under Section 2.[13]

-- Thus, the intentional breach of a binding commitment intended to restrain the acquisition and exercise of monopoly power has been held to constitute exclusionary conduct when such conduct is found to have occurred as part of a scheme to acquire monopoly power. For instance, in *Hewlett-Packard Co. v. Boston Scientific Corp.*, 77 F. Supp. 2d 189 (D. Mass. 1999), the plaintiff alleged that in order to secure FTC approval of a proposed transaction, the defendant made express, binding commitments in a consent order to take certain actions to facilitate post-merger entry and competition. After the merger was completed the defendant failed to live up to these commitments. By doing so, the defendant acquired monopoly power that it would not have possessed had it adhered to the terms of the consent order. The court held that such allegations, if proven, would support a Sect. 2 claim.

-- In *Biovail Corp. Int'l v. Hoechst Aktiengesellschaft*, 49 F.Supp. 2d 750 (D.N.J. 1999), the court reached the same conclusion on similar facts. The FTC conditioned approval of a merger between Hoechst and Marion Merrell Dow (MMD) in part on the merged company's agreement to give Biovail a right of reference to data filed with the FDA in support of MMD's Cardizem, for approval of Biovail's competing generic drugs. Hoechst initially agreed and gave Biovail a right of reference, in a letter to the FDA, but it subsequently narrowed the scope of its commitment to the FDA; as a result, one of Biovail's applications for a drug to compete with Cardizem was denied for lack of supporting data. Biovail then sued Hoechst, alleging that it had intentionally reneged on its commitment to the FTC in order to win approval for its merger with MMD. The court

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11 Creighton *et al.*, *supra*, 72 Antitrust L.J. at 988-89.

12 *Id.*

13 M. S. Royall and A. Di Vincenzo, "The FTC's N-Data Consent Order: A Missed Opportunity to Clarify Antitrust in Standard Setting," ANTITRUST, Vol. 22, No. 3, 83-92, at 86-87 (Summer 2008).

stated that if Biovail could show that the defendants narrowed the right of reference in order to keep Biovail's competing generic product from being approved, this would support a claim under Section 2 that defendants were willfully seeking to maintain or obtain monopoly power in the relevant market.[14]

-- Repudiation of a F/RAND commitment to an SSO is also similar to the installed-base opportunism found to be exclusionary in the Supreme Court's decision in *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451 (1992). Kodak, after first allowing independent service organizations to purchase Kodak replacement parts for its copiers, subsequently altered its policy to permit only Kodak-licensed service agents to purchase replacement parts for its copiers. Because non-Kodak copier repair service providers were unable to obtain spare parts as a result of the new policy, the policy change effectively eliminated competition from that segment of the market. Kodak's ex post conduct was found to be exclusionary because it foreclosed competition in copier repair services through a policy change that could not have been reasonably foreseen by Kodak's copier customers when they purchased the copiers, with attendant 'lock-in' effects.

The Court held that Kodak's opportunistic about-face after consumers had made significant and irreversible investments in its copiers could be a basis for a finding that Kodak engaged in exclusionary conduct under Section 2 – and this in the absence of any allegation of deception on the part of Kodak, such as, for instance, an intent to lure prospective customers into buying Kodak copiers with the prospect of obtaining independent servicing, then to be followed by a policy change, thereby ensuring lock-in. Similarly, as alleged in the petition, to cite one example, manufacturers of digital transmission and demodulation equipment relied on the ATSC standards – just like their customers, the networks and cable companies – for their purchasing decision. By the time Rembrandt had allegedly repudiated the F/RAND commitment, both manufacturers and their customers were locked in by their investments.

Rembrandt's repudiation was effectively a policy change by the current obligor (Rembrandt), but of course with no deception on its part as of the time the original commitment by AT&T was given, nor indeed with no necessary pleading of deception at the time Rembrandt assumed the obligation. Thus, hold-up conduct by a PAE fits within the category of installed-based opportunism/exclusionary conduct outlined in *Kodak* – a policy change that could not have been reasonably anticipated by those dependent on its intellectual property and does not necessarily include initial deception on the part of the defendant. A theory of Section 2 liability for installed-base opportunisim should apply with even more reason in a standard setting context, given the implications of lock-in and consumer harm from a repudiation of F/RAND commitments.

Distinguishable from exploitation of legitimately acquired monopoly power. Exclusionary conduct in the form of hold-up by a PAE is distinguishable from another form of exploitation – not exploitation of opportunistic behavior, as described above, but exploitation of monopoly power that has been legitimately acquired. To shed some light

[14] *Id.* at 766.

on this distinction, reference to the appellate decision in *Rambus v. FTC* is helpful (although there is considerable disagreement – which I share – with the court's holding and various aspects of its rationale). The Court of Appeals concluded that Rambus was a lawful monopolist because the FTC did not show that but for Rambus's failure to make the necessary disclosure, JEDEC would have selected an alternative technology. The court reasoned that a lawful monopolist's raising prices, even allegedly in violation of a F/RAND obligation, does not violate antitrust law because it has no effect on competitive structure. Under this analysis, whatever Rambus's sins of commission or omission, JEDEC still might have chosen its technology; thus, its conduct did not exclude any other technology in the competition for the standard. Rather, at most, Rambus's conduct enabled it to charge a higher price than what might be reasonably construed by a court to be "reasonable and nondiscriminatory." Assuming, *arguendo*, that the court was correct – and I do not think that it was – that Rambus was therefore a lawful monopolist, then its conduct could therefore be characterized as exploitative but not exclusionary or violative of the antitrust laws. As the court stated, "deceit merely enabling a monopolist to charge higher prices than it otherwise could have charged . . . would not in itself constitute monopolization." It further explained: "an otherwise lawful monopolist's use of deception simply to obtain higher prices normally has no particular tendency to exclude rivals and thus to diminish competition."[15]

Unlike the Court of Appeals' characterization of the facts in *Rambus*, the petition regarding Rembrandt alleged that there were alternative, viable technologies to the one chosen for the ATSC digital transmission standard. Thus, even assuming that the framing of the case by the Court of Appeals in Rambus was correct – that the FTC had to show, but could not show, that *but for* Rambus's alleged omission, JEDEC would have selected another technology – the conduct by Rembrandt, and that of any other similarly situated PAE, is clearly distinguishable. Rembrandt did not legitimately acquire a monopoly and then merely 'exploit' that power by refusing to grant a license to the manufacturers on F/RAND terms and instead suing the end-user networks (and cable companies) for infringement. Rather, Rembrandt illegitimately acquired monopoly power and exercised that power by repudiating the F/RAND commitment.

The distinction between NYNEX's legitimate acquisition of monopoly power in *NYNEX v. Discon*, on which the Court of Appeals relied in *Rambus*, and the unlawful acquisition of such power by Rembrandt or similarly situated PAE, lies in the distinction, with particular application to standard setting, between monopoly and monopoly power.

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[15] The court relied for this proposition principally on the Supreme Court's decision in *NYNEX v. Discon*. NYNEX had a lawfully secured monopoly with attendant monopoly power, which was then subjected to a regulatory regime intended to limit what NYNEX could charge for certain services. The Court held that a fraudulent scheme by NYNEX to increase prices did not violate the antitrust laws because the consumer harm stemmed, not from a "less competitive market," but from market power that was "lawfully in the hands of the monopolist." NYNEX's wrongful conduct thus had no nexus to its initial acquisition of monopoly power. In contrast, Rambus obtained monopoly power by deceptively inducing the SSO participants into believing that its non-disclosure obviated the need to demand a F/RAND commitment from it, as a means to prevent the creation of monopoly power. Rambus thus did not have monopoly power prior to the inclusion of its technology in the standard, and this distinction from NYNEX is crucial.

On the allegations in the petition, the prior owners of the asserted SEP (the '627), assuming they claimed it to be essential to the standard, and until assignment to and repudiation by Rembrandt, had a monopoly in the relevant market because of the adoption of the standard; but they did not have monopoly *power*, because their power to exploit the monopoly through supracompetitive pricing, or even through declining to license the technology, was constrained by the F/RAND commitment. In this sense it may be said that the prior owners of the asserted SEP, the '627, in giving and/or abiding by the F/RAND commitment, 'negotiated away' the monopoly power they otherwise would have derived from the asserted inclusion of their IP in the standard. When Rembrandt then rejected this constraint, according to the petition, it engaged in illegal monopolization. Once having been assigned the patent and acceded to the monopoly position corresponding to it because of the adoption of the standard, Rembrandt opportunistically exploited the monopoly when it repudiated and breached the F/RAND commitment. In this way, Rembrandt willfully acquired and exercised monopoly power in the relevant market in violation of Section 2, according to the petition – and so also would be the case with any similarly situated PAE that engages in patent hold-up.

Thus, in the rather narrow sense in which exploitation of legitimately acquired monopoly power may be viewed as not anticompetitive, the alleged conduct of Rembrandt, as with any similarly situated PAE engaged in patent hold-up, is not exploitative but instead exclusionary, as it is properly understood as affecting the competitive structure *ab initio* (in effect, retroactively) for the selection of the technology to be encompassed by the standard.

2. The need for government antitrust enforcement regarding hold-up by PAEs in lieu of/in addition to action on the contract or other common law cause of action.

Although the thrust of this comment is directed to the viability of Section 2 claims for hold-up by PAEs, a word is in order regarding the need for government intervention on such matters generally, although this topic has been addressed by other participants and commentators.

Some may suggest that there may be little need for government antitrust enforcement regarding hold-up by PAEs because private non-antitrust remedies are available and the immediately affected firms are often sophisticated high technology companies.[16] But such a view is misconceived for several reasons. First, the interests of the firms facing licensing demands based on opportunistic conduct are not necessarily coincident with the interests of consumers. The entities facing the licensing demand may be able simply to pass on the licensing fees through the cost of the end product. Thus, their primary concern might not be that they have to pay the licensing fee but rather that they not have to pay a fee substantially higher than their rivals. They may be willing to be victimized by the exercise of monopoly power as long as they are not placed at a

[16] As Creighton *et al.* put it, rhetorically, "One may question the role antitrust law should play in cheap exclusion cases, given that other legal theories, such as contract or tort, often will provide some form of redress (at least to potential victims)." 72 Antitrust L.J. at 993.

competitive disadvantage. "[W]hen a standard used in a fairly competitive industry is subject to *uniform* hold-up [and as distinguished from hold-up of a single firm], direct buyers may bear little of the costs, which falls primarily on final consumers."[17] Thus, "private litigation may not vindicate the same set of public interests that are addressed by the Sherman Act or Section 5 of the FTC Act."[18]

Second, the firms facing such licensing demands may have a variety of arrangements with the firm engaging in the opportunistic conduct and thus may not have a complete incentive to attack this opportunistic conduct. Practitioners in private antitrust class action litigation often observe that the "small victims" in the market bring these cases because the larger victims may have a variety of arrangements with the antitrust violator that they do not want to place at risk.

Third, the legal remedies for the firms facing licensing demands may be inadequate. As former Competition Bureau Director Creighton has observed, business torts and other remedies are "imperfect substitutes for government antitrust enforcement." In the standard setting area in particular, because of collective action and free rider problems, and the possible defenses such as reasonable reliance, "standard-setting participants, victims though they may be, [are] imperfect substitutes for government enforcement."[19]

Fourth, the firms subject to the licensing demand may not have the resources or assets necessary to vindicate their rights in court. The firms making the licensing demands may initially focus on relatively weak market participants hoping to extract a favorable settlement from those unable to mount the litigation battle. Some firms may have no choice but to capitulate to the anticompetitive conduct and the cost of the opportunistic conduct may eventually be passed on to the end consumer.

Fifth, the firms facing licensing demands may also hold patents essential to the standard and be in a position to profit from engaging in comparable opportunistic conduct. In other words, those who are best positioned to bring a private cause of action may prefer to divide the "monopoly spoils" with other essential patent holders by all engaging in opportunistic conduct, as this may be a more profitable strategy than filing a lawsuit to reign in the conduct of others.

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[17] J. Farrell, J. Hayes, C. Shapiro and T. Sullivan, "Standard Setting, Patents, and Hold-Up," 74 Antitrust L.J. 603, 645 (2007). As the authors explain, the reason for this is that "[i]f each direct buyer knows that its rivals are paying as high a royalty as it is, pass-through can largely immunize it against economic loss from high running royalties. Thus, the direct buyers, who might otherwise be the best guardians against gratuitous insertion of patents in standards, or against excessive royalties from such patents, may bear very little of the harm. [. . .] Thus, consumers are not, in general well protected by the self-interest of direct technology buyers." *Id.*

[18] A.F. Abbott and T.A. Gebhard, "Standard-Setting Disclosure Policies: Evaluating Antitrust Concerns in Light of *Rambus*," 16 Antitrust ABA 29, 33 (Summer 2002) (citing this point as one of the policy justifications for an administrative remedy in *Rambus*).

[19] Susan A. Creighton *et al.*, "Cheap Exclusion," 72 Antitrust L.J. 975, 993-94 (2005).

Finally, the FTC and DOJ are best positioned to clarify the law and defend the public interest in the area of opportunistic conduct involving standards, given the expertise and resources at their disposal. The agencies' economic and legal expertise and panoply of powers make them uniquely well suited to address the competitive problems arising from standard setting, including hold-up by PAEs.[20]

Thank you for the opportunity to submit this comment.

Sincerely,

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[20] As Creighton *et al.* summarize the point: "Antitrust advances certain policy goals and vindicates certain interests, notably the interest in protecting the competitive process and thereby garnering economic benefits for consumers. It is not at all clear that the business tort and other [no-antitrust] remedies . . . are well designed to protect those interests and advance those goals. Nor is it clear that the parties in a position to pursue those remedies possess the right incentives or motivation. For example, in the standards-setting arena . . . , numerous issues including collective action and free-rider problems, the availability of defenses such as a 'reasonable' reliance burden that would not apply to a government enforcement action, and the opportunity to pass hold-up costs through to consumers, all render standard-setting participants, victims though they may be, imperfect substitutes for government antitrust enforcement." *Id.* at 994 (citations omitted).