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# Antitrust Issues in IP Settlements

*Part One of a Two-Part Series*

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## INTRODUCTION

While courts generally favor the settlement of intellectual property disputes, these settlements, which often include exclusive licenses, cross-licenses, and pooling arrangements, may implicate antitrust concerns. For example, the Department of Justice (“DOJ”) opened an antitrust investigation last year into a proposed settlement between Google and a class of authors and publishers in a copyright infringement class action, *The Authors Guild, Inc. v. Google Inc.*, Civil No. 1:05-CV-8136 (S.D.N.Y.). The DOJ expressed concern that the settlement restricted price competition among authors and publishers and granted Google *de facto* exclusive rights over the digital distribution of millions of orphan and rights-uncertain works, effectively precluding other digital distributors from competing with Google. The parties proposed an amended agreement last November, but the DOJ found that the modified agreement continues to raise antitrust concerns by, *inter alia*, “confer[ring] significant and possibly anticompetitive advantages on a single entity — Google ... [as] the only competitor in the digital marketplace with the rights to distribute and otherwise exploit a vast array of works in multiple formats.” See DOJ, Statement of Interest of the United States of America Regarding Proposed Amended Settlement Agreement (Feb. 4, 2010), at 2, *available at* [www.justice.gov/atr/cases/f255000/255012.pdf](http://www.justice.gov/atr/cases/f255000/255012.pdf). As a result, final settlement in the case has been substantially delayed.

To avoid potential antitrust liability and additional costly litigation, it is important to recognize the antitrust issues implicated in settlement agreements involving intellectual property rights. The inquiry into whether a given settlement and its particular terms are anticompetitive is highly fact-intensive and generally requires a “rule of reason” analysis, by which the reviewing court or agency weighs the terms’ anticompetitive effects against their pro-competitive benefits. In certain limited circumstances where a practice is so plainly anticompetitive that no effects inquiry is necessary, the settlement terms can be deemed *per se* unlawful, such as agreements among competitors to fix prices or to allocate markets. Such “naked” restraints have no legitimate, pro-competitive purpose.

With this framework in mind, we discuss below some common IP settlement terms that may give rise to antitrust liability. While not intended as an exhaustive list, these licenses and arrangements exemplify the types of provisions that are likely to raise antitrust concerns.

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## **EXCLUSIVE LICENSES AND EXCLUSIVE DEALING**

Although expressly permitted by the Patent Act, 35 U.S.C. § 261, exclusive licensing of all intellectual property, including patents, is not immune from antitrust scrutiny. If the exclusive license involves setting prices, limiting quantities or output, or dividing a market, then the antitrust risks are generally higher than if the settlement involves either an exclusive license that did not contain such restrictions or a non-exclusive license.

Exclusive dealing arrangements arise where a license restrains a licensee's ability to deal in competing technologies. These restraints, which may foreclose access to inputs, raise prices, or limit output, are analyzed under the rule of reason, considering key factors, such as the duration of the exclusive dealing arrangement, the degree of foreclosure, and characteristics of the input and output markets. *See, e.g., Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961); DOJ & FTC, *Antitrust Guidelines for the Licensing of Intellectual Property* (Apr. 6, 1995) [hereinafter "*Guidelines*"] § 5.4. As exemplified by the DOJ's concerns with the Google books settlement discussed above, exclusive dealing arrangements need not be explicit and may be found to fall outside the typical licensing context if the agreement has the practical effect of excluding competitors from a market.

## **PRICE, QUANTITY, OR OUTPUT RESTRAINTS**

With respect to restraints on price, in *United States v. General Electric Co.*, 272 U.S. 476, 480-90 (1926), the Supreme Court held that where both parties are horizontal competitors that manufactured a patented product, the licensor may fix the price at which the licensee must sell it. Criticized for giving naked price-fixing antitrust immunity in the context of an intellectual property licensing agreement, the *General Electric* doctrine has been narrowed over the years and does not apply to pooling arrangements or the granting of multiple licenses containing price restrictions. *See, e.g., United States v. New Wrinkle, Inc.*, 342 U.S. 371 (1952); *Newburgh Moire Co. v. Superior Moire Co.*, 237 F.2d 283 (3d Cir. 1956). While the Supreme Court in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007), reversed long-standing precedent in subjecting minimum resale price restraints to a rule of reason analysis, the turbulence created by *Leegin* suggests that vertical restraints created by patent licenses may still pose a liability risk. In fact, earlier this year, two congressional committees approved bills (H.R. 1390 and S. 148) that would overturn *Leegin* and reinstate a *per se* ban on vertical price-fixing. In 2009, Maryland was the first state to enact *Leegin* repealer legislation, making vertical price-fixing *per se* illegal under the Maryland Antitrust Act. *See* S.B. 239 (Md. 2009)

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(repealing and re-enacting, with amendments, Md. Code Ann., Com. Law § 11-204), available at <http://mlis.state.md.us/2009rs/bills/sb/sb0239t.pdf>. In other states, such as New York and California, vertical pricing restraints may be prohibited under those states' existing antitrust laws, independent of federal antitrust law. See Alan M. Barr, State Challenges to Vertical Price Fixing in the Post-*Leegin* World (May 21, 2009), at 3-4, available at <http://www.ftc.gov/opp/workshops/rpm/may09/docs/abarr.pdf>.

Horizontal restraints on quantity or output also deserve close antitrust scrutiny because absent the existence of the exclusive patent license, such restraints may be *per se* illegal under the antitrust laws. Where a valid patent right exists, however, quantity and output restraints are likely to be viewed under the rule of reason. See, e.g., *Atari Games Corp. v. Nintendo of Am., Inc.*, 897 F.2d 1572, 1578 (Fed. Cir. 1990); *Tex. Instruments, Inc. v. Hyundai Elecs. Indus. Co.*, 49 F. Supp. 2d 893, 915 (E.D. Tex. 1999); *United States v. E.I. DuPont de Nemours & Co.*, 118 F. Supp. 41, 226 (D. Del. 1953), *aff'd on other grounds*, 351 U.S. 377 (1956). Agreements that prohibit an alleged infringer from manufacturing, selling, or using products that extend beyond the patent at issue also may raise antitrust concerns. See *Dole Refrigerating Co. v. Kold-Hold Mfg. Co.*, 185 F.2d 809, 816-17 (6th Cir. 1950).

#### **TERRITORIAL, CUSTOMER-BASED, AND FIELD-OF-USE RESTRAINTS**

Although expressly authorized by the Patent Act, territory-restricted licenses, along with customer-based and field-of-use restrictions, may raise antitrust concerns because, absent a valid patent or legitimate infringement dispute, a naked horizontal agreement to restrict the territories in which a licensee can sell (or to limit the customers or fields of use with which it can deal) would amount to a *per se* illegal market division agreement. Such restraints in the intellectual property context are likely to be analyzed under the rule of reason (see, e.g., *Carter v. Variflex, Inc.*, 101 F. Supp. 2d 1261, 1264-66 (C.D. Cal. 2000); *Clorox Co. v. Sterling Winthrop, Inc.*, 117 F.3d 50, 55-56 (2d Cir. 1997)); however, they will be deemed *per se* unlawful if used merely as a sham to conceal a price-fixing or market allocation agreement (see *In re Cardizem CD Antitrust Litig.*, 105 F. Supp. 2d 682, 693-707 (E.D. Mich. 2000), *aff'd*, 332 F.3d 896 (6th Cir. 2003); *Guidelines* Example 7, at 17).

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## CROSS-LICENSING AND POOLING ARRANGEMENTS

Cross-licensing and pooling arrangements occur when members of a group of intellectual property owners agree to combine their rights by jointly waiving or granting rights to their respective intellectual property. These cross-licensing and pooling arrangements often have restrictions on who may join the pool and sometimes include the creation of special holding companies. While these arrangements can have pro-competitive benefits and promote innovation, they also may raise anticompetitive concerns when they act as an attempt to share in an unlawful monopoly or as a device to exclude competitors from markets. *See, e.g., Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100 (1969); *Honeywell, Inc. v. Sperry Rand Corp.*, No. 4-67 Civ. 138, 1973 U.S. Dist. LEXIS 15600 (D. Minn. Oct. 19, 1973). When evaluating whether these arrangements violate the antitrust laws, the reviewing court or agency “will consider whether the effect of the settlement is to diminish competition among entities that would have been actual or likely potential competitors in a relevant market in the absence of the cross-license. In the absence of offsetting efficiencies, such settlements may be challenged as unlawful restraints of trade.” *See Guidelines* § 5.5, at 28. In *United States v. Singer Manufacturing Co.*, 374 U.S. 174 (1963), for example, the Supreme Court found that a settlement of a patent dispute that took the form of a cross-license agreement between several different producers of sewing machines was anticompetitive because it acted to exclude Japanese competitors.

## CONCLUSION

Whether a settlement agreement violates the antitrust laws depends on many factors that are specific to the underlying facts. An important first step in the analysis, however, is recognizing and understanding the potential antitrust implications of IP settlement agreements. In the next piece of our two-part series, we will discuss recent challenges by the government and private plaintiffs to settlements between brand name and generic drug manufacturers. These challenges have further refined the antitrust framework for analyzing patent litigation settlement agreements in the pharmaceutical industry.

## ABOUT THE AUTHOR

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