

The Particular Antitrust Concerns with Patent Acquisitions

**Ilene Knable Gotts***

Wachtell, Lipton, Rosen & Katz, New York
ikgotts@wlrk.com

**Scott Sher**

Wilson Sonsini Goodrich & Rosati, Washington, DC
ssher@wsgr.com

If recent events are any indication, the use of patents in ‘nuclear warfare’ among companies in technology-based industries is unlikely to end soon. Under the current marketplace dynamics, for a company to be able to compete in high-tech industries such as operating systems (OS) on mobile devices, it must have a large patent portfolio to defend itself against the inevitable lawsuits that competitors bring to impose a significant tax on – or even ultimately to prevent the entry of – new products on the market. Without the ability to bring about ‘mutually assured destruction’, a company has no way to defend itself against costly patent litigation. The problem is exacerbated because, as one commenter put it, ‘ridiculous, broad, meaningless patents get approved all the time’.¹ In 2011, the US Patent and Trademark Office approved a record 247,713 patents, up from 244,341 patents in 2010, which was up from 191,927 patents in 2009 (an almost 30 per cent increase over two years).² In many cases, these patents are not being sought to reward innovation but as a means to impede it.

In a report published in March of 2010, the Federal Trade Commission (FTC) recognised that competition is distorted when existing patents are valued based on the ability to extract rents from companies that have already implemented the technology.³ Contrary to its underlying intent, the current patent system produces less competition and innovation given the fierce patent battles presently being waged:

- small startups get sued for patent infringement before bringing their products to market and as a result cannot bring their products to market, are delayed in bringing their products to market, can only bring their products to market at higher prices, or must be acquired by a larger competitor with a significant patent portfolio that can be

asserted defensively in order to bring their products to market;

- the offering and adoption of open source alternatives is stifled because companies implementing open source technologies fear patent claims;
- large companies spend billions of dollars on patent acquisition and litigation rather than on bringing new products to market; and
- consumers are faced with higher prices and fewer choices because new products either never make it to market or only arrive after significant delay.

As acting Assistant Attorney General Sharis Pozen stated in her last official speech in the position:

‘The intersection of [competition law and intellectual property law] is significant because so many of our most important inventions and technologies rely heavily on patents and other forms of IP. These rights grant control over important inventions and technologies and create salutary innovation incentives. However, antitrust enforcement remains critical in these sectors to ensure that IP rights are not abused to limit competition.’⁴

An even more troubling trend for antitrust regulators is the rise of competitors joining together to purchase patent portfolios. On one side, these consortia argue that allowing the companies to come together to purchase portfolios allows them to cross-license the patents among themselves, preventing costly patent litigation. Conversely, companies left out of the consortium are deprived of any means of defending themselves against the assertion of the group’s patents. Two recent patent acquisitions by a group consortium of competitors are illustrative: (i) CPTN Holdings LLC’s acquisition of Novell, Inc’s patents; and (ii) Rockstar Bidco’s US\$4.5bn bid for Nortel Network’s

patents after the company filed for bankruptcy. As discussed further below, such acquisitions are subject to review under section 1 of the Sherman Act as well as section 7 of the Clayton Act.

In addition, an acquisition or transfer of existing patents is subject to review under section 7 as well. Recently, the DOJ investigated Google's acquisition of Motorola Mobility under section 7.⁵ Moreover, the acquisition of patents by non-practicing entities (ie, 'patent trolls') may raise significant competition and policy concerns that will require careful consideration by antitrust agencies.

Finally, as discussed below, the focus on the acquisition of patents necessary to implement a recognised industry standard (standard essential patents (SEPs)), as opposed to patents needed to commercialise a standards-compliant device that were not formally contributed to a standard setting organisation (SSO), is in all likelihood too narrow and may need to be further refined by the antitrust agencies as they continue to explore these patent acquisition issues.

Legal and statutory framework

It is important to understand first the statutory and regulatory principles under which patent acquisitions are reviewed. The Antitrust Division of the US Department of Justice (DOJ) and the FTC have expressly stated that '[t]he Agencies apply the same general antitrust principles to conduct involving intellectual property that they apply to conduct involving any other form of tangible or intangible property'.⁶ And while it is true that patents confer a statutory right to exclude others from the use of a given technology:

'[a]n intellectual property owner's rights to exclude are similar to the rights enjoyed by owners of other forms of private property. As with other forms of private property, certain types of conduct with respect to intellectual property may have anticompetitive effects against which the antitrust laws can and do protect. Intellectual property is thus neither particularly free from scrutiny under the antitrust laws, nor particularly suspect under them.'⁷

Thus, the purchase of intellectual property rights (including patents), where such acquisition would tend to enhance or entrench the purchaser's market power in a properly defined relevant market, is an example of anti-competitive conduct involving intellectual property that justifies enforcement activity by the DOJ.

Analysis under section 1 of the Sherman Act

It also is axiomatic that competitors cannot band together to exclude another competitor: such conduct would violate section 1 of the Sherman Act.⁸ Thus, any investigation of patent consortia – where those consortia consist of competitors – also must be analysed under section 1 to determine whether the combination was formed in an effort to exclude a party that did not participate in a consortium.

As far back as the decision in *United States v Singer Manufacturing Co*,⁹ the US Supreme Court has held that it is unlawful for competitors concertedly to use patents to hinder or exclude a competitor from the market. In *Singer*, three parties – the leading makers of sewing machines – conspired concerning potential litigation with respect to the parties' patents and patent applications in the United States.¹⁰ After entering into a series of cross licences, one of the firms raised the possibility that, 'having arrived at their respective agreements, [they] should act in concert in prosecuting their patents against all others in the field'.¹¹ Thereafter, the parties engaged in a course of conduct that achieved precisely the end suggested by one of the group's members: the exclusion of 'their common competitors, the Japanese manufacturers'.¹²

One of the defendants argued that the licence served the purpose of allowing the manufacturers to practice their inventions free of infringement claims from the others. The court found this position unconvincing:

'[The] fact that the enforcement plan likewise served Singer is of no consequence, the controlling factor being the overall common design, *i.e.*, to destroy the Japanese sale of infringing machines in the United States by placing the patent in Singer's hands the better to achieve this result. . . . [I]t [was] this concerted action to restrain trade, clearly established by the course of dealings, that condemn[ed] the transactions under the Sherman Act.'¹³

Analysis under section 7 of the Clayton Act

Patent acquisition can also raise concerns under section 7 of the Clayton Act. As in all acquisitions, where the acquisition of patents confers market power on the acquirer and there is a likelihood of a substantial lessening of competition, the acquisition violates the law. Nevertheless, there are a number of important considerations specific to the context of patent acquisitions that bear on the analysis of a transaction's potential competitive effect. These include:

- Whether the acquisition confers a blocking position to the acquiring party in a technology market, such that the acquirer would be able to exclude competitors from a goods market or would be able to use its patent position to raise the costs of rivals. Such was the case in the DOJ's suit to prevent 3D Systems, Incorporated (3D Systems) from acquiring DTM Corporation (DTM). Absent the merger, neither 3D Systems nor DTM individually had the ability to block a competitor from the market but when the patents were combined, 3D Systems would hold a blocking position and have the unilateral ability to foreclose competition.¹⁴ The DOJ therefore required 3D Systems and DTM to license their rapid prototyping patents to a third-party competitor that would compete in the US market as part of the settlement.¹⁵
- Whether the acquisition contributes a 'patent thicket' that makes it impractical for competitors to determine whether their activity infringes the acquiring party's large patent portfolio. Recent patent acquisitions by Apple, Microsoft, Facebook and others have included thousands of patents. Ascertaining whether the acquired patents are complete or partial substitutes for those in the acquiring party's own portfolio – and thus whether a blocking position may be created – requires a detailed examination of each patent. Both the antitrust agencies and smaller competitors are at an extreme disadvantage in conducting this inquiry for large patent portfolios. Thus, even the determination that the acquisition results in the accumulation of too many patents in a particular technology field may lead the agencies to conclude third parties would be deterred from entering the market or competing, and thus confers market power to the acquiring party.
- Whether the acquiring party has different incentives with regard to the patents than the selling firm. For example, if an acquiring party competes in a goods market against potential infringers, it may be more likely to enforce those patent rights against potentially infringing competitors (as a way to gain an upper-hand in the goods market) than the party that sold the patents. Another example would be if the acquiring party was a 'patent troll' that does not create any products that practice the patent. In such an instance, the troll may have a stronger incentive to extract monopoly rents from infringers because it is not susceptible to counterclaims for infringement.

Issues related to remedies

It is also essential to understand the remedies available to antitrust agencies to correct anti-competitive behaviour or prevent the anti-competitive abuse of market power. Where an acquisition of intellectual property raises competitive concerns, remedies must be tailored specifically to the potential anti-competitive outcome and strong enough to alleviate such issues. These principles are reflected in the DOJ's updated policy guide to merger remedies (the Guide), issued on 17 June 2011.¹⁶ As indicated in the Guide:

'[T]he touchstone principle for the Division in analyzing remedies is that a successful merger remedy must effectively preserve competition in the relevant market.... In horizontal merger matters, structural remedies often effectively preserve competition, including when used in conjunction with conduct provisions. Structural remedies may be appropriate in vertical merger matters as well, but conduct remedies often can effectively address anticompetitive issues raised by vertical mergers. In all cases, the key is finding a remedy that works, thereby effectively preserving competition in order to promote innovation and consumer welfare.'¹⁷

The Guide further indicates that the central goal 'is preserving competition, not determining outcomes or picking winners and losers'.¹⁸ The Guide points out that vertical mergers 'can create changed incentives and enhance the ability of the merged firm to impair the competitive process. In such situations, a remedy that counteracts these changed incentives or eliminates the merged firm's ability to act on them may be appropriate'.¹⁹ The Guide recognises a wide variety of conduct remedies that may help to preserve competition: '[t]he most common forms of conduct relief are firewall, non-discrimination, mandatory licensing, transparency, and anti-retaliation provisions, as well as prohibitions on certain contracting practices'.²⁰ As the Guide acknowledges, however, 'No matter what type of conduct remedy is considered... a remedy is not effective if it cannot be enforced'.²¹

The remainder of this article will focus on recent DOJ statements regarding the role of licensing commitments for patents, including SEPs,²² in alleviating the competitive concerns raised in patent portfolio acquisitions.

Recent enforcement activity

By way of background, smartphones are one of the newest consumer products to have gained widespread popularity. Google, Apple, Microsoft and RIM, among others, have each developed mobile operating systems for

smartphones and tablets. Apple and RIM manufacture and sell devices that use their own mobile OS. Microsoft does not manufacture mobile devices; instead, it derives revenues by licensing its operating systems, Windows Phone 7 and Windows Mobile, to wireless handset original equipment manufacturers (OEMs). Google provides its Android OS under an open source licence free of charge for all OEMs that may want to use it. Today there are approximately 40 different manufacturers of Android devices, all with different features and price points. At the beginning of 2010, both Microsoft and Apple started to assert their extensive patent portfolios against OEMs that used Android in lawsuits and other proceedings that sought to block the sale of Android products. At the time, Google had only about 1,000, the majority of which covered search technologies, and was in no position to bring counterclaims on a similar scale.

Three significant patent portfolios with potential implications for the smartphone industry became available for purchase in 2010 and 2011. In the first case, CPTN – a holding company equally owned by Microsoft Inc, Oracle Corp, Apple Inc and EMC Corp – agreed in November 2010 to acquire approximately 450 patents from Novell in connection with Novell's merger with Attachmate Corporation. The acquired patents relate to Linux, the open source platform that underlies many consumer electronics products and forms the technological basis of the Android operating system. The agreement raised antitrust concerns in part because each of CPTN's owners had a history of attacking open source software projects through patent litigation.

In light of these concerns, the Open Source Initiative and Free Software Foundation opposed the transaction, noting that the sole or leading competition to the owners of CPTN for some products is open source alternatives.²³ Because open source software has been such an important force in encouraging competition in the technology industry, the DOJ opened an investigation to study the competitive effects of the patent acquisition. After the initiation of that investigation, CPTN agreed to make several changes to the agreement with Novell to address competition concerns:

- Microsoft would sell back to Attachmate all of the Novell patents that Microsoft would otherwise have acquired, and receive a license for the use of those patents acquired by the other three CPTN owners and any patents retained by Novell;
- EMC would not acquire 33 Novell patents related to virtualisation software;
- all of the Novell patents would be acquired subject to the GNU General Public License and a licence to the Open Invention Network (OIN), a significant conglomeration of patents designed to allow OIN members to defend the Linux ecosystem; and

- neither CPTN nor its owners would make any statement or take any action to influence or encourage either Novell or Attachmate to modify which of the patents are available under the OIN licence.²⁴

The DOJ indicated that the acquisition as originally proposed would have allowed the consortium 'to jeopardize the ability of open source software, such as Linux, to continue to innovate and compete in the development and distribution.... of desktop and mobile operating systems'.²⁵ Nor was the DOJ convinced that the changes to the deal made by the CPTN members would entirely allay its concerns. DOJ Acting Assistant Attorney General Sharis Pozen noted:

'To promote innovation and competition, it is critical to balance antitrust enforcement with allowing appropriate patent transfers and exercise of patent rights.... Although we recognize that the various changes to the agreement recently made by the parties are helpful, the department will continue to investigate the distribution of patents to ensure continued competition.'²⁶

In the second transaction, the trustee of the Nortel Networks bankruptcy estate announced in May 2011 that over 6,000 patents belonging to Nortel would be auctioned off.²⁷ These patents have potentially far-ranging applications in mobile devices. Some of these patents related to wireless video, wi-fi communication, internet search, social networking and fourth-generation mobile data technology, commonly referred to as LTE. Google became the 'stalking horse' bidder on 4 April 2011.²⁸ In June 2011, however, Apple and Rockstar Bidco (which consisted of Microsoft, RIM, Sony and Ericsson) jointly outbid Google to acquire the patents.²⁹

Finally, on 15 August 2011, Google proposed purchasing Motorola Mobility Holdings, Inc, one of the manufacturers of handsets that makes use of the Android OS. Google immediately committed to running Motorola as a separate business. Google indicated that its primary interest in Motorola was the acquisition of the company's extensive patent portfolio to defend the Android ecosystem from patent attacks by aggressors seeking to raise the costs of the Android OS to OEMs and, in turn, the cost of the Android devices for consumers. According to the DOJ, Motorola holds about 17,000 issued patents and 6,800 applications, including several SEPs relevant to wireless devices that Motorola Mobility has committed to license through its participation in Standards Setting Organisations (SSOs).

In a closing statement issued on 13 February 2012, the DOJ disclosed the analysis that it undertook in connection with Microsoft's purchase of some of the Novell patents, the Apple/Rockstar purchase of

Nortel's patents, and Google's acquisition of Motorola Mobility.³⁰ As a starting proposition, the DOJ recognised that a patent gives the owner the right to exclude infringing devices from the market as well as to charge royalties to firms that it chooses to permit to make, use and sell devices that would otherwise infringe the patents. The DOJ was particularly focused on the patents considered SEPs due to their inclusion by SSOs in technical standards for essential components of wireless technology. Although most SSOs require the owners of SEPs to make disclosures and commit to license SEPs on reasonable and nondiscriminatory (RAND) terms, in practice such RAND requirements have not always prevented significant disputes from arising in connection with the licensing of SEPs.³¹

The closing statement indicates that the DOJ's investigation focused on whether the acquiring firms would have the incentive and ability to exploit ambiguous and vague RAND licensing commitments to hold up rivals, thus preventing or inhibiting innovation and competition. As the DOJ indicated:

‘Such hold up could include raising costs to rivals by demanding suprareactive rates, compelling prospective licensees to grant the SEP holder the right to use the licensee’s differentiating intellectual property, charging licensees the entire portfolio royalty rate when licensing only a small subset of the patent holder’s SEPs in its portfolio, or seeking to prevent or exclude patents practicing those SEPs from the market altogether.’³²

The primary concern expressed in the DOJ's closing statement is how the proposed transactions might change the incentive and the ability for acquiring firms to use SEPs in that way.

The DOJ concluded that each of the transactions was unlikely to substantially lessen competition for wireless devices. First, the DOJ stated that RIM's and Microsoft's low market shares in mobile platforms would likely render unprofitable a strategy to harm rivals either through injunctions or suprareactive rivals based on the acquired Nortel SEPs because they would not attract a sufficient number of new customers to compensate for the lost patent royalty revenues.³³ Also, according to the DOJ, Microsoft has cross-licence agreements in place with the majority of its Android-based OEM competitors, making such a strategy less likely.

By contrast, the DOJ concluded that Apple's and Google's substantial share of mobile platforms makes it more likely that they would hold up rivals. The specific transactions at issue, however, are not likely to substantially lessen competition. The evidence showed that Motorola had been aggressive in its intellectual property prosecutions, making it unlikely that a shift in ownership to Google, which has never asserted a patent

claim unless sued on patents by the opposing party first, would lead to even more aggressive enforcement.³⁴ With respect to Apple's acquisition of Novell patents, the patents have already been committed to an open source community that requires patent holders to offer a perpetual royalty-free licence for use in the Linux system, and Apple has agreed to honour those commitments.³⁵

The curious distinction between SEP and essential, non-standards based patents and the transfer of patents to non-practice entities

Under section 7 of the Clayton Act, the antitrust agencies ask whether a transaction is likely to result in a substantial lessening of competition; the same is true under analogous European Commission law.³⁶ The important element in that inquiry is whether the acquisition gives the acquiring firm the *ability* and *incentive* to exercise market power.³⁷ The DOJ – in connection with its review of recent patent acquisitions described above – posited that the acquisition of SEPs gives a firm a greater *ability* to exercise market power than essential but non-standards based patents. As described below, that conclusion may be both over-and under-inclusive, capturing transactions that do not confer market power and also missing transactions that do confer market power. Equally important, but to date less explored, is the *incentive* to exercise market power. As we explain, the transfer of SEPs (and essential non-standards based patents) to non-practicing entities, for example, could confer both the *incentive* and *ability* to the non-practicing entity to exercise market power.

The distinction between SEPs and essential, non-standards based patents

In its analysis of the transactions, the DOJ took into account the public statements made by Apple, Google and Microsoft regarding their SEP licensing practices. Both Apple and Microsoft made clear that they would not seek to prevent or exclude rivals' products from the market in exercising their SEP rights. If these positions were adhered to in practice, the DOJ opined that the possibility of a hold up or use of an injunction would be significantly reduced. According to the DOJ, the Google commitment did not go as far in connection with the exercise of newly acquired patent rights but it eliminated any merger specific-concerns.³⁸

It is curious, however, that the DOJ limited its concerns to patents that the companies had agreed to license through SSOs. There is generally no guarantee that firms will submit any or all of their patents that might be necessary to implement a standard to the relevant SSO:³⁹ a firm that owns a patent necessary to implement a standard may well decide that the

benefits of unrestricted licensing (which may allow the patentee to attain higher rates by threatening hold up) outweigh the benefits of inclusion in the SSO's official list of SEPs. In addition, complex consumer products, such as mobile phones, often incorporate patents that do not read on an officially recognised standard but are essential as a practical matter to build interoperable devices and services. Indeed, both Apple's and Microsoft's patent portfolios appear to contain a number of such *de facto* essential patents.

There is no reason that the acquisition of officially recognised SEPs should cause more concern for antitrust authorities than the acquisition of non-SEP patents necessary to implement a standards-compliant device. In both cases, patentees are able to take advantage of the 'fundamental transformation' that renders alternative technologies less attractive once a particular technology is adopted as a standard and firms make technology-specific investments to implement it.⁴⁰

As then-Chairman Majoras of the FTC noted:

'Early in the standardization process, industry members might easily be able to abandon one technology in favor of another. But once the level of resources committed to the standard rises and the costs of switching to a new technology mount, industry members may find themselves locked into using the chosen technology.'⁴¹

The holders of patents necessary to implement a standard are able to extract higher licence fees than they would have been able to negotiate prior to the licensor's investments in the chosen technology. Whether the patent is licensed through an SSO or directly by the patentee is irrelevant to the incentives and economic factors that create the danger of anti-competitive licence rates.

There is nothing about inclusion in an SSO-administered standard that renders SEPs more susceptible to hold up than other patents that read on industry standards. In fact, many SSOs have disclosure, negotiation and licensing rules intended to mitigate the holdup problem.⁴² Although these rules are by no means a complete solution (particularly when, as described below, such SEPs are transferred to patent trolls),⁴³ they provide at least some check against anti-competitive behaviour. Essential patents that are not included in an SSO-standard are not subject to this check and non-members are not bound by an SSO's rules governing disclosure and licensing.

The FTC has recently acknowledged the risks posed by third-party essential patents to firms producing products that may infringe those patents. In May 2011, the FTC announced a project to investigate the risks of patent holdup resulting from the inclusion of patented technologies in collaborative standards.⁴⁴ Recognising

the absence of protections against holdup and standard manipulation by non-members, the commission invited comment on the question of whether there are 'mechanisms for an SSO to encourage disclosure of relevant patents or patent applications held by nonmembers'. This inquiry suggests that the FTC recognises the anti-competitive threat posed by essential patents not licensed through an SSO. In addition, the DOJ has noted similar problems may arise 'where a patent holder's prior actions, such as open source commitments, lead others to make complementary investments'.⁴⁵ This statement acknowledges the potential anti-competitive effects of a patent holder exploiting lock in without reference to the standard-setting process at all. There is no compelling economic distinction between the patent holder in the DOJ's statement, which creates its own lock in by misleading others, and a third-party holder of an essential patent which takes advantage of the lock in created by an adopted standard.

Nevertheless, the DOJ limited its investigation in these transactions to only SEPs already encumbered by RAND commitments and considered whether such patents would change the incentive or ability for the acquirers to hold up competitors. The DOJ focused particularly on whether or not the additional patents would increase the likelihood that the acquiring firms would seek an injunction or exclusion order. It is difficult to see how SEPs with RAND commitments are always going to be more likely than any other essential patent to lead to anti-competitive holdup through the threat of injunctive relief. The DOJ's focus is particularly striking in this instance as both Apple and Microsoft have explicitly stated that seeking an injunction or exclusion order is inconsistent with a commitment to RAND licensing.⁴⁶ Moreover, to date only one court has issued an injunction related to an SEP,⁴⁷ and that case involved a defendant that flatly refused to negotiate with the patent holder. Injunctions or exclusion orders appear to be a much more significant threat in the case of essential patents not licensed through an SSO and subject to RAND commitments.

The fact that an acquired patent portfolio is already part of a standard and subject to RAND commitments does not itself raise concerns over and above the acquisition of any other essential patent. Patents that are essential, whether or not they are officially incorporated into an established standard, can give patentees considerable market power. The standardisation process is imperfect and may fail to incorporate every essential patent, even if each holder of such a patent were willing to join. Consequently, both SSO members and third-party patentees are capable of abusing the investments that other firms make in adopting a standard, and the antitrust agencies should not limit their inquiry to SEPs when considering the competitive impact of patent acquisitions.

The transfer of patents to non-practicing entities

That is not to say that the acquisition of SEPs could not raise significant antitrust problems, particularly where the acquisition was designed to evade previously agreed upon RAND terms. For example, it is reported that Google recently filed a complaint with the European Commission against Nokia and Microsoft, apparently alleging that the decision to transfer Nokia's SEPs to a third party – MOSAID – violates competition laws, as the sale to MOSAID was simply a means to avoid Nokia's previously agreed upon RAND commitments.⁴⁸

Transferring patents to a troll could raise concerns. For example, consider the firm that makes commitments to license its SEPs to third parties at RAND rates. In reliance upon those RAND commitments, SSOs may incorporate those SEPs into various standards. Those RAND commitments impede that firm's ability to bring litigation against competitors that had incorporated its SEPs into their technology. The subsequent transfer of those patent rights – including SEPs – to a non-practicing entity whose sole purpose is to seek royalties for patents it owns or acquires, could result in that firm seeking higher royalty rates, and more frequently, than the prior owner.

This raises an important issue: when does the transfer of patents to a non-practicing entity raise competition concerns? The transfer of SEPs to a non-practicing entity could facilitate the exercise of market power.⁴⁹ How? Because patent trolls, unlike a firm that manufacturers and sells products, can enforce patents without fear of a patent countersuit and the need to consent to cross-licences because patent trolls, by their very nature, do not make products and therefore cannot be sued for infringement. This gives a patent troll a greater ability to seek higher royalties for the SEPs received from the original owner than if the patents had remained in the original owner's hands because the original owner (a manufacturer and seller of goods) would need to deal with the consequences of its decision to seek higher royalties (ie, it would face counter claims from the parties it decided to sue for infringement).⁵⁰

Moreover, the transfer of SEPs to non-practicing entities raises other, related concerns. Non-practicing entities do not contribute technology to, or participate in, SSOs and thus can enforce patents without concern that SSOs might decline to accept future technological contributions in response to opportunistic patent enforcement. Additionally, non-practicing entities have the ability to exploit the high cost of patent litigation to extract economic rents that can be well above the economic value of the patents involved. The cost of defending suits often exceeds the reasonable royalties

of a patent in suit. This could make it rational for the target of the infringement suit to settle for an amount far above the economic value of the patents.⁵¹ This becomes more likely when the owner of the patents is a patent troll: without the concern that it will be subject to patent counterclaims (because it does not manufacture anything that can infringe), non-practicing entities more often will have the ability to extract rents above those than a firm that manufactures and sells products can reasonably expect (as manufacturers face risk of counterclaims if they bring an infringement suit).⁵²

Given the proliferation of wireless and smartphone technology, which is both extremely profitable and the subject of countless patents, this issue only is going to grow in importance in the near future.

Conclusion

Only time will tell whether the recent patent portfolio activity fosters competition by creating a détente in the patent wars and the DOJ's intervention helped to deter patent aggression. As the DOJ acknowledged, determining the correct balance between the rightful exercise of patent rights and a patent holder's incentive and ability to harm competition through the anti-competitive use of those rights requires a complex and potentially far-reaching inquiry. It is unclear, however, why the DOJ chose to limit its concerns to SEPs (which the SSO has ensured does not provide an opportunity for hold up through the enforceable contractual obligations of its members) and not focused at all on non-SEP patents that may also be essential to build interoperable products and services. Such *de facto* essential patents are just as capable of being used by the patent holder to engage in hold up and harm competition in downstream markets. It appears that the Apple and Microsoft patent portfolios contain many instances of this type of patent, which makes this concern more than just theoretical. In this vein, it is worth noting that just days before the issuance of the closing statement, Apple commenced yet another lawsuit against Motorola seeking to exclude yet more devices from the United States which suggests that peace is not imminent for all the parties involved.⁵³ Another issue with these current patent acquisitions is the sheer number of patents involved. The agencies will have to grapple with the issue of whether the accumulation of too many patents in a particular technology field deters third parties from entering the market or competing, by creating a patent thicket that confers market power to the acquiring party.

The acquisition and assertion of IP rights represents a significant present and future battlefield in technology markets. Because the patent system in the United States

currently is unable to manage the number of filings or make substantive determinations of the validity of patents prior to their issuance, the cost of the assertion of those IP rights will continue to rise. If something is not done about the patent system as it now operates, the antitrust authorities will need to continue to police both the assertion of transfer of IP rights to ensure that they are not put to anti-competitive ends.

About the authors

A member of Wachtell, Lipton, Rosen & Katz's Antitrust Department, **Ilene Knable Gotts** represents and counsels clients on a range of antitrust matters, particularly those relating to mergers and acquisitions. Ms Gotts was the Chair of the Antitrust and Trade Regulation Section of the Federal Bar Association from 1995–1997 and Chair of the Antitrust Section of the New York State Bar Association in 2005–2006. Ms. Gotts served as Chair of the American Bar Association Section of Antitrust Law in 2009–2010, having previously served in a number of positions including the International Officer and Chair of the Mergers Committee. Ms Gotts is regularly recognised as one of the world's top antitrust lawyers, including being selected in the 2007–2012 editions of *The International Who's Who of Business Lawyers* as one of the top 15 global competition lawyers, in the first tier ranking of *Chambers USA Guide*, and as one of the 'leading individuals' in PLC *Which Lawyer Yearbook*. Ms Gotts serves as the co-editor of *Competition Law International* and on the advisory boards of *Antitrust and Trade Regulation Report*, *Antitrust Counselor*, and *Antitrust Report*.

Scott Sher is a partner in Wilson Sonsini Goodrich & Rosati's Washington, DC, office, where his practice focuses on antitrust counseling and litigation. He represents technology clients in connection with antitrust issues that arise throughout the merger and acquisition process, from pre-merger counseling through investigations conducted by the Department of Justice, the Federal Trade Commission and foreign regulatory agencies. In addition, Scott has significant experience providing both day-to-day counseling and litigation representation to clients on issues pertaining to joint ventures, the Robinson-Patman Act, pricing and distribution, trade association and patent pooling matters, and the Sherman Act.

Notes

- * The authors and their firms were involved in some of the transactions discussed herein. The views that are expressed, however, are not to be attributed to the firms or to any of the firms' clients, but are solely the personal views of the authors and the information contained herein are from public sources only. The authors would like to thank Brad Tannis, an associate in the Washington, DC office of Wilson Sonsini Goodrich & Rosati, for his assistance with the drafting of this article.
- 1 Mike Masnick, 'When Patents Attack: How Patents Are Destroying Innovation in Silicon Valley', *Techdirt* (25 July 2011), available at: www.techdirt.com/articles/20110724/22250715225/when-patents-attack-how-patents-are-destroying-innovation-silicon-valley.shtml.
- 2 'Google's Motorola Deal Shows Need for Better Patent System', *Bloomberg* (18 August 2011), available at: www.bloomberg.com/news/2011-08-19/google-s-motorola-deal-shows-need-to-develop-better-patent-system-view.html. See also, US Patent and Trademark Office, *US Patent Statistics Chart Calendar Years 1963–2011*, (27 March 2012), available at: www.uspto.gov/web/offices/ac/ido/oeip/taf/us_stat.htm.
- 3 Fed'l Trade Comm'n, *The Evolving IP Marketplace, Aligning Patent Notice and Remedies with Competition* (2011), available at: www.ftc.gov/os/2011/03/110307patentreport.pdf.
- 4 Sharis A Pozen, Acting Ass't Atty Gen, Antitrust Division, US Dep't of Justice, *Promoting Competition and Innovation Through Vigorous Enforcement of the Antitrust Laws on Behalf of Consumers*, Remarks as Prepared for the Brookings Institution, Washington, DC (23 April 2012), at p 17, available at: www.justice.gov/atr/public/speeches/282515.pdf.
- 5 Around the time we are writing this article, there have been additional 'single buyer' patent acquisitions announced. In March 2012, Facebook indicated that it was acquiring 750 patents from TBM (Facebook had recently been sued for patent infringement by Yahoo). On 10 April 2012, Microsoft proposed acquiring and licensing AOL's patent portfolio; on 23 April 2012, Facebook proposed acquiring most of these AOL patents from Microsoft. Those acquisitions had not been reviewed by the antitrust authorities as of this writing and are, therefore, outside of the scope of our discussion.
- 6 *US Dep'l of Justice & Fed'l Trade Comm'n Antitrust Guidelines for the Licensing of Intellectual Property*, section 2.1 (6 April 1995), available at: www.justice.gov/atr/public/guidelines/0558.htm.
- 7 *Ibid.*
- 8 15 USC, section 1.
- 9 374 US 174 (1963).
- 10 See *Ibid.* at 175.
- 11 *Ibid.* at 181.
- 12 *Ibid.* at 189.
- 13 *Ibid.* at 195.
- 14 Press Release, US Dep't of Justice, *Department of Justice Requires 3D Systems Corporation and DTM Corporation To Lift Patent Entry Barriers* (16 August 2001), available at: www.justice.gov/atr/public/press_releases/2001/8810.htm.
- 15 *Ibid.*
- 16 *US Dep'l of Justice, Antitrust Division, Antitrust Division Policy to Merger Remedies* (2011), available at: www.justice.gov/atr/public/guidelines/272350.pdf.
- 17 *Ibid.* at 1-2.
- 18 *Ibid.* at 3.
- 19 *Ibid.* at 5.
- 20 *Ibid.* at 13. Mandatory licensing provisions can also alleviate competitive concerns in a conventional merger context by enabling competitors access to a key input. See, for example, Press Release, US Dep't of Justice, *Justice Department Requires Google Inc to Develop and License Travel Software in Order to Proceed with Its Acquisition of ITA Software Inc* (8 April 2011), available at: www.justice.gov/opa/pr/2011/April/11_at_445.html; Press Release, *US Dep't of Justice, Justice Department Allows Comcast-NBCU Joint Venture to Proceed with Conditions* (18 January 2011), available at: www.justice.gov/opa/pr/2011/January/11-at-061.html. Recently, press reports indicate that the DOJ's conditions have resulted in AEG's launching of a new ticketing site. See Rob Cox, *Blocking a Deal Isn't Always Best Antitrust Answer, Breaking News* (30 September 2011),

- available at: <http://blogs.reuters.com/columns/2011/09/30/blocking-a-deal-isn%E2%80%99t-always-best-antitrust-answer/>. In addition, for a discussion of licensing and other remedies to address concerns that arise in a conventional merger context in which innovation plays an important role, see Michael L Katz and Howard A Shelanski, 'Mergers and Innovation', 74 *Antitrust LJ* 1 (2007). Some of the recent consents include not only a licence for technology, but the right to purchase the technology or to transfer the licence to a third party later. In addition, nondiscrimination provisions have been included to incorporate the concepts of equal access, equal efforts, and equal terms.
- 21 See note 16 above, at 13.
- 22 Although the recent DOJ statements do not mention the 'essential facilities' doctrine, the approach taken by the enforcement agency resembles earlier precedent under the doctrine. As a general proposition, companies are under no antitrust obligations to sell or license their products to, or provide their assets for use by, another company. *United States v Colgate & Co*, 250 US 300, 307 (1919); accord *Verizon Commc'n Inc v Law Offices of Curtis v Trinko, LLP*, 540 US 398 408 (2004). The exceptions to this general proposition are quite limited, primarily involving changes in access to the input by a firm with market power or control by a monopolist of an essential facility. See Christine A Varney, Ass't Atty Gen, Antitrust Div, US Dep't of Justice, *Vigorous Antitrust Enforcement in this Challenging Era* (12 May 2009), available at: www.justice.gov/atr/public/speeches/245777.htm. The owner of the property remains entitled to reasonable compensation for use of the asset. See P Areeda and H Hovenkamp, *Antitrust Law* p 774e (2009); Donald I Baker, 'Compulsory Access to Network Joint Ventures under the Sherman Act: Rules or Roulette?', 1993 *Utah L Rev* 999 (1993); OECD Policy Roundtables, *The Essential Facilities Concept* (1996), at 89.
- 23 See Brett Smith, *OSI and FSF Send Joint Position to the Department of Justice* (20 January 2011), available at: www.fsf.org/news/osi-fsf-joint-position-cptn.
- 24 Press Release, US Dep't of Justice, *CPTN Holdings LLC and Novell Inc Change Deal in Order to Address Department of Justice's Open Source Concerns* (20 April 2011), available at: www.justice.gov/opa/pr/2011/April/11-at-491.html.
- 25 *Ibid.*
- 26 *Ibid.*
- 27 *Intellectual Asset Management Blog* (14 May 2011), see: http://giplg.com/images/stories/Articles/05142010_iam_nortelseekingbuyers.pdf.
- 28 Kent Walker, *Google Blog* (4 April 2011, 10:45 AM), <http://googleblog.blogspot.com/2011/04/patents-and-innovation.html>.
- 29 Press Release, Nortel, *Nortel Announces the Winning Bidder of its Patent Portfolio for a Purchase Price of US\$4.5 Billion* (30 June 2011), available at: www2.nortel.com/go/news_detail.jsp?cat_id=8055&oid=100272428.
- 30 Press Release, US Dep't of Justice, *Statement of the Department of Justice's Antitrust Division on its Decision to Close its Investigations of Google Inc's Acquisition of Motorola Mobility holdings Inc and the Acquisitions of Certain Patents by Apple Inc, Microsoft Corp, and Research in Motion Ltd* (13 February 2012), available at: www.justice.gov/atr/public/press_releases/2012/280190.htm.
- 31 The EU has also been looking at the role of SEPs in smartphones in conduct investigations involving Samsung and Microsoft. In a speech to the European Parliament on 28 February 2012, European Commission Vice President Joaquin Almunia indicated: 'Standards are essential in this industry, because different devices can work with each other only thanks to commonly agreed technologies. And because to build a modern smart phone one needs thousands of standard-essential patents, their holders often have considerable market power. Any company that holds these patents can effectively hold up the entire industry with the threat of banning the products of competitors from the market. This sort of hold-up is not acceptable.' Speech by Joaquín Almunia, Vice President of the European Commission Responsible for Competition Policy Competition Policy and Growth, before the European Parliament, Internal Market and Consumer Protection Committee, 28 February 2012, available at: <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/12/131>.
- 32 See note 30 above; see also Richard J Gilbert, 'Deal or No Deal? Licensing Negotiations in Standard-Setting Organizations', 77 *Antitrust LJ* 855 (2011).
- 33 See note 30 above.
- 34 *Ibid.*
- 35 *Ibid.*
- 36 See *US Dep't of Justice & Fed'l Trade Comm'n, Horizontal Merger Guidelines* (2010), available at: www.justice.gov/atr/public/guidelines/hmg-2010.html.
- 37 *Ibid.*
- 38 *Ibid.*
- 39 See Mark A Lemley, 'Intellectual Property Rights and Standard-Setting Organizations', 90 *U Calif L Rev*, 1889, 1961 (2002).
- 40 Oliver Williamson, *The Economic Institutions of Capitalism: Firms, Markets, and Relational Contracting*, 61-63 (1985).
- 41 Deborah Platt Majoras, Chairman, Fed Trade Comm'n, *Recognizing the Procompetitive Potential of Royalty Discussions in Standard Setting* (23 September 2005).
- 42 See Joseph Farrell et al, 'Standard Setting, Patents, and Hold-Up', 74 *Antitrust LJ* 603, 609 (2007).
- 43 In its announcement that it would close its investigations into Google's acquisition of Motorola Mobility and Rockstar Bidco's acquisition of the Nortel patents, the DOJ noted that RAND commitments '[i]n practice... have not prevented significant disputes from arising in connection with the licensing of SEPs, including actions by patent holders seeking injunctive or exclusionary relief that could alter competitive market outcomes.' Press Release, see note 30 above.
- 44 *Request for Comments and Announcement of Workshop on Standard-Setting Issues*, 76 Fed Reg 28,036 (13 May 2011).
- 45 See note 30 above.
- 46 *Ibid.*
- 47 *Commonwealth Scientific and Indus. Research Org v Buffalo Tech (USA), Inc*, 492 F Supp 2d 600 (ED Tex 2007).
- 48 See, for example, John Letzing, 'Google Points Finger at Microsoft, Nokia', *Wall Street Journal* (31 May 2012), available at: <http://online.wsj.com/article/SB10001424052702304821304577438740232322350.html>.
- 49 The DOJ, FTC and Commission have clearly recognised this contention. For instance, in a recent speech, Joaquin Almunia noted that '[t]he potential abuses around standard-essential patents are illustration of this concern.... Owners of such standard essential patents are conferred a power on the market that they cannot be allowed to misuse.' Speech, Joaquin Almunia, Vice President of the European Commission responsible for Competition Policy, *Que vadis Europa? New Frontiers of Antitrust 2012* (10 February 2012), available at: <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/12/83&format=HTML&aged=0&language=EN&guiLanguage=en>.
- 50 As the FTC notes, 'patent litigation or royalty payments increase the manufacturer's costs and risk, deterring innovation.... The potential for later patent assertions creates a risk that a manufacturer's costs will increase and its return on investment will decrease after it has developed and commercialized a product.' See note 3 above.
- 51 Discussing the costs of defending patent suits, 'Mr. Myrvold [, of Intellectual Ventures,] acknowledges facing resistance from companies he targets for licenses. But his patent inventory gives him leverage to extract settlements without litigation. "I say, I can afford to sue you on all of these, and you can't afford to defend on all these." See, for example, Amol Sharma and Don Clark, 'Tech Guru Riles the Industry By Seeking Huge Patent Fees', *Wall Street Journal* (17 September 2008), available at: <http://online.wsj.com/article/SB122161127802345821.html>.
- 52 See James Bessen, Jennifer Ford and Michael J Meurer, *The Private and Social Costs of Patent Trolls*, Boston University School of Law Working Paper, (19 September 2011), available at: www.cato.org/pubs/regulation/regv34n4/v34n4-1.pdf.
- 53 Dan Levine, 'Apple Sues Motorola Mobility over Qualcomm License', *Reuters* (10 February 2012, 5:50 PM): www.reuters.com/article/2012/02/10/us-apple-motorola-lawsuit-idUSTRE8191SV20120210.