Introduction

We are pleased to bring you the first edition of WSGR's Antitrust Wire, the WSGR Antitrust Group newsletter. In this issue, we address recent developments in the antitrust laws, including issues relating to the settlement of patent litigation, mergers, standard-setting and resale price maintenance. This newsletter touches on several issues that our antitrust attorneys tackle on a daily basis for WSGR’s clients.

As a strategic business partner to its clients, WSGR’s Antitrust Group advises clients on the full range of antitrust issues, including vertical restrictions, pricing, joint ventures and strategic alliances, worldwide compliance with premerger notification requirements, merger counseling, licensing restrictions and antitrust litigation. Our attorneys and staff are among the most experienced in the country on antitrust issues facing our high technology clients. The Group regularly represents technology companies in antitrust merger reviews pending before the U.S. Department of Justice, the Federal Trade Commission and the European Commission, and our antitrust litigators extensively practice in federal and state courts around the country.

FTC Challenges Patent Settlement Agreements

By David A. Killam
Denise L. Diaz

Direct competitors often find themselves entangled in costly and time-consuming patent litigation. Settling such suits is generally in the interest of the parties and the judicial system. Nevertheless, agreements among competitors to settle patent litigation can draw antitrust scrutiny. Indeed, just this month the Federal Trade Commission (FTC) launched a suit against three drug manufacturers for entering into allegedly anticompetitive settlement agreements.

On April 2, 2001, the FTC charged Schering-Plough Corporation, Upsher-Smith Laboratories and ESI Lederle, Inc. (ESI), a division of American Home Products Corporation (AHP), with violating Section 5 of the FTC Act by entering into settlement agreements aimed at keeping low-cost generic drugs out of a market dominated by Schering. In a 5-to-0 decision the agency charged that Schering illegally paid Upsher-Smith and AHP millions of dollars to induce them to delay launching their
generic versions of Schering’s K-Dur 20, a widely prescribed potassium chloride supplement.

According to the FTC’s administrative complaint, Upsher-Smith sought approval to manufacture and distribute a generic version of K-Dur 20 from the Food and Drug Administration (FDA). Schering promptly responded by filing a patent infringement suit against Upsher-Smith. The parties subsequently settled this suit.

Under the challenged settlement agreement, Upsher-Smith agreed not to sell a generic version of K-Dur 20 — regardless of whether the product infringed any Schering patent — until September 2001. Upsher-Smith also licensed Schering to market five Upsher-Smith products. Schering in turn agreed to pay Upsher-Smith $60 million, but the FTC alleged that the $60 million payment “was unrelated to the value of the products Upsher-Smith licensed to Schering.” According to the complaint, “Schering never sold four of the five licensed products, made minimal sales of the fifth, and has no expectation of making additional sales of any of the five products.” The FTC thus concluded that the parties had colluded to keep generic drugs out of the market, and charged them accordingly.

The Commission also challenged a settlement agreement between Schering and another potential entrant, AHP. AHP, through ESI, filed an application seeking approval from the FDA for a generic version of K-Dur 20. Soon after ESI filed its application, Schering sued ESI for patent infringement. The parties eventually settled their dispute.

Like Upsher-Smith, ESI agreed to grant Schering licenses to two of its generic products. In return, Schering agreed to pay ESI an additional $15 million for the licenses. According to the FTC’s complaint, however, Schering made no sales of the two products it licensed from ESI. The complaint charges that payments ostensibly made for these licenses were in fact to secure ESI’s agreement to delay entering the market and were not based on the value of the licensed products.

The lesson to be learned from the FTC’s case against Schering, Upsher-Smith and AHP is not that settlement agreements among competitors are necessarily anticompetitive. Most settlement agreements — even those involving direct competitors embroiled in patent litigation — do not raise serious antitrust concerns. Rather, the lesson to be learned is that the antitrust laws are implicated when direct competitors contemplate collaboration in any context. Early identification and analysis of potential antitrust issues thus is critical to the success of any venture among competitors even if that venture involves the settlement of a patent suit.

♦

Upcoming Events

May 3-4, 2001
Philadelphia, PA
“Intellectual Property and Antitrust: Navigating the Minefield”
Susan A. Creighton will speak on “Navigating the Antitrust Risks Associated with Licensing Restrictions, Package Licensing, Cross-Licensing and Patent Pools” with other renowned practitioners.

May 7-8, 2001
Washington, D.C.
“Emerging Issues for Competition Policy in the World of E-Commerce”
The FTC will hold a two-day public workshop to examine selected issues of competition policy arising in connection with B2B and B2C exchanges. The FTC invited Chris Compton to speak at the workshop.

May 15, 2001
New York, NY
Antitrust & Trade Regulation Committee
David A. Killam will speak on “Current Topics in Mergers” with FTC Commissioner Thomas Leary and others.

June 14-15, 2001
Palo Alto, CA
“Handling Mergers & Acquisitions in High-Tech and Emerging Growth Environments”
Susan A. Creighton will speak on the antitrust issues arising from transactions in high-tech industries.
The Perils of Standard-Setting

By Charles T.C. (Chris) Compton
Scott A. Sher

In the new economy where technology is constantly and rapidly developing, many businesses—oftentimes competitors—come together to coordinate the development of standards for these technologies. Such cooperation is efficient, and frequently essential for the rapid development of interoperable products and protocols. However, such “standard-setting” can also lead to antitrust scrutiny from both the government and from companies developing competing technology. In fact, two recent actions and an ongoing Federal Trade Commission investigation against one prominent high technology company suggest that the courts and agencies are pressing the outer reaches of antitrust liability.

In August 2000, Hyundai Electronics Industries and Micron Technology, Inc. brought separate lawsuits against Rambus Inc., alleging that Rambus violated the antitrust laws by improperly manipulating the standard-setting process. Infonwin has filed a similar suit, which is set for trial in the next month. These suits were in response to litigation previously initiated by Rambus, alleging that Hyundai, Micron and several other companies infringed several of Rambus’s patents relating to synchronous DRAM (SRAM) high-speed memory technology and the memory and logic chips implementing that technology.

Hyundai and Micron alleged that Rambus violated the rules of the Joint Electronic Devices Engineering Council (JEDEC) Solid State Technology Association, the semiconductor engineering standardization body. In the early 1990s, JEDEC coordinated the development of technology standards for SRAM, so that memory from different suppliers would be compatible with each other and with the modules and systems that use SRAM.

According to the complaints, Rambus, as a member of JEDEC, attended the meetings where the standards were set. However, “instead of participating in the JEDEC standard-setting process in good faith, Rambus allegedly subverted the process, using this collaboration with its competitors to secure market power” by failing to disclose to JEDEC the existence of patent rights and patent applications that would leave susceptible to claims of infringement, products that relied upon the JEDEC standards. The complaint alleges that, after the standard was adopted, Rambus brought infringement actions against companies such as Hyundai and Micron that had developed products following the JEDEC standards in violation of the antitrust laws.

Both district court judges have allowed these antitrust claims to proceed, concluding that “a defendant’s failure to disclose relevant patent rights to a standard-setting body and subsequent assertion of those rights against other members of the body may constitute an antitrust violation under Section 2 of the Sherman Act.” The FTC has recently launched its own investigation based upon these allegations.

Litigation claims, of course, are not proven facts and Rambus is vigorously contesting these cases. The cases illustrate, however, why participants in standard-setting need to consider the implications of their intellectual property rights.

There are several other crucial antitrust issues that confront standard-setting organizations and their members. Associations must be wary about sharing competitively sensitive information, and must be careful to draft clear guidelines governing the methods by which the association will set standards. Such organizations must have clear policies that are applied evenly to all members, and must recognize that where the organization is not open to all affected members of the business community, it may be vulnerable to charges of “group boycott” or unfair competition. Of course, standard-setting is essential to the new economy, but it must be done correctly, and businesses must be cognizant of how to avoid antitrust scrutiny and litigation.
Minimum Resale Price Maintenance Programs

By David A. Killam
Scott A. Sher

Free-riding discounters can wreak havoc with a manufacturer’s distribution chain. They often refuse to invest in an infrastructure that will provide adequate customer support, choosing instead to attract customers by offering deep discounts at the expense of distributors who make significant investments in the sale of the manufacturer’s product or services. As a result, legitimate resellers who charge higher resale prices to pay for such support and service lose sales to the discounters. Additionally, those customers who purchase from the discounting resellers are often dissatisfied with the product because that crucial support and service is missing; this, in turn, damages the reputation of the manufacturer, and hurts its competitive position.

What should a manufacturer do in such a circumstance? How about arranging with their distributors and resellers to set a minimum resale price (minimum resale price maintenance or RPM) or minimum advertised prices (MAP) is considered vertical price fixing, and is per se unlawful. Simply put, if a court concludes that such a policy exists, no further inquiry is required into the effects of such a policy—it automatically violates the Sherman Act.

There are, however, more creative ways to set up such a program that may provide greater protection from antitrust liability (although not ironclad). Manufacturers can make such a policy “unilateral.” That is, they can establish such a program as long as they receive no input from any

(continued)
of their distributors. Alternately, under carefully crafted policies, manufacturers can condition the availability of cooperative advertising funds on resellers advertising their price at a suggested minimum price. An even safer solution allows manufacturers to establish a “National Accounts Programs,” whereby they distribute directly to customers and bypass the discounters entirely.

Does the government care about RPM? You bet it does. The Justice Department and the Federal Trade Commission both have recently challenged MAP and RPM programs vigorously under the per se rule. See, e.g., In the Matter of Time Warner, Inc. et. al, 2000 WL 1257799, No. 971-0070 (F.T.C. Aug. 30, 2000); Reebok Int'l Ltd., 5 Trade Reg. Rep. (CCH) 23,813 (F.T.C. July 18, 1995). Do private parties care? Of course. Disgruntled resellers who lose their profit margins, as well as customers and shareholders have commenced litigation. In fact, shareholders and customers have commenced massive class action litigation within the last year—seeking significant damages stemming from the challenged RPM and MAP programs.

Dealing with difficult resellers is crucial to a successful business. However, businesses must be aware that the antitrust laws do not always, at first blush, directly correlate to good business sense. Those businesses considering any pricing programs should consult with antitrust counsel before they decide to implement them. Ideally, antitrust counsel can help draft creative solutions to these problems that provide some protection from government or private party treble-damages litigation.

### FTC Seeks to Unwind Three-Year Old Merger

**By Charles T.C. (Chris) Compton**

Denise L. Díaz

Seeking to unwind a merger that closed three years ago, the Federal Trade Commission (FTC) filed a civil action against The Hearst Trust earlier this month. The FTC has asked a federal court in Washington, D.C. for the extraordinary remedies of divestiture of the company acquired by Hearst and disgorgement of profits. The Commission also seeks an order imposing fines of $11,000 per day from the closing date for Hearst’s alleged failure to fully comply with the premerger filing requirements imposed by the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act) and its implementing regulations.

The Commission’s complaint challenges Hearst’s 1998 acquisition of Medi-Span, Inc. According to the complaint, Medi-Span was the chief competitor of First DataBank, Hearst’s wholly owned subsidiary, in the market for comprehensive integratable drug information databases. The FTC alleges that the acquisition gave First DataBank monopoly power in the market, resulting in “drastic price increases to customers, and reductions in product quality and customer service.” The agency further alleges that “the acquisition took place after Defendant Hearst failed to produce documents required by the HSR Act for the Commission’s premerger review of the proposed acquisition.” The FTC charges Hearst with violations of Section 5 of the FTC Act, Section 7 of the Clayton Act as well as the HSR Act.

The Hearst case, though it entails a belated challenge and attempt to unwind a merger that is claimed to lessen competition, really has arisen because of the failure of the parties—who went through a normal HSR review—to submit all of the required documents. Independent of Clayton Act Section 7 issues for a merger that “tends substantially to lessen competition,” failure to comply with the HSR Act enables the agency to seek an unwinding of the deal, disgorgement of profits and a fine of $11,000 (now $12,000) per day since the violation occurred. The FTC in Hearst seeks a fine of about $30 million—more than the value of the merger.

The FTC vote on this action was 3-to-2. However, even the dissenters differed only on the profit disgorgement remedy, not on the need for an enforcement action. The case serves as an unpleasant reminder of: (1) the disastrous consequences that can befall a party who fails to fully comply with premerger notification requirements; and (2) the ability of antitrust agencies to challenge a merger even after it closes.
Charles T.C. (Chris) Compton

Chris is a litigator specializing in antitrust and trade regulation issues. He cut his teeth on the watershed IBM antitrust cases in the late 1970s at O'Melveny & Myers. In 1980, he joined Wilson Sonsini Goodrich & Rosati and started the Firm’s antitrust practice. Since then, he has overseen more than 600 successful Hart-Scott-Rodino filings, many of which involved formal investigations by the Federal Trade Commission, Department of Justice, and international antitrust agencies. None of these transactions has ever been blocked or abandoned due to antitrust challenge.

In addition to a wide range of intellectual property litigation, including Lotus v. Borland, Chris has handled more than 20 antitrust suits involving alleged price discrimination, refusals to deal, distributor terminations, group boycotts, monopoly, state law Cartwright Act claims, grand jury investigations, and price fixing.

Chris wrote the Firm’s Antitrust & Trade Regulation Primer for attorneys and clients. He has written a number of articles for various publications, including “The Changing U.S. View of Joint Ventures: Permission to ‘Walk with the Devil’ published in 26 International Business Lawyer 129 (March 1998) and Where Now for Microsoft? published in Global Competition Review December 1999/January 2000, page 27.

He is an Adjunct Professor at Santa Clara University School of Law. He has lectured at Boalt Hall and is a regular speaker at conferences in the United States and Europe on antitrust, intellectual property and mergers and acquisitions.

Chris received his law degree in 1968 from New York University School of Law, where he was a Root-Tilden Scholar and Managing Editor of the Law Review. He served in the Air Force JAG Corps as a Military Judge, having earned his Bachelor of Science degree (with honors) from the United States Air Force Academy in 1965.

Outside the office, Chris has served as President of the Palo Alto Area Bar Association, Kids In Common, an advocacy effort on behalf of at-risk children, and the Law Foundation of Silicon Valley. Chris serves as an arbitrator for the American Arbitration Association’s Large Complex Case Program and the Asia Pacific Center.

Chris is admitted to practice in California and the District of Columbia, as well as in several United States District Courts, the U.S. Court of Appeals for the Ninth Circuit, the U.S. Court of Military Appeals and the United States Supreme Court.

If you would like to add your name to our mailing list, please e-mail antitrust@wsgr.com. To remove your name from our mailing list, please e-mail antitrust@wsgr.com with “remove” in the subject line.

THIS INFORMATION IS NOT INTENDED AS PROFESSIONAL ADVICE FOR ANY PARTICULAR SITUATION.