

Patent Pools and Antitrust Enforcement – 1997-2001

Christopher J. Kelly

Kaye Scholer LLP

FTC-DOJ Hearings on Competition and
Intellectual Property Law and Policy
in the Knowledge-Based Economy

April 17, 2002

Summary of Presentation

- Patent pool analysis
- The three DOJ pools
- What they stand for
- Unresolved issues

Patent Pools – the old view

- Anathema to antitrust law
 - *United States v. Line Material Co.*, 333 U.S. 287 (1948)
 - <http://caselaw.lp.findlaw.com/scripts/getcase.pl?navby=case&court=us&vol=333&page=287>
 - Really about RPM, not pools!
 - *But cf.* Aircraft Manufacturers' Pool (1918)
 - Klein, "Cross-Licensing and Antitrust Law," June 1997
 - <http://www.usdoj.gov/atr/public/speeches/1123.htm>

DOJ-FTC IP Licensing Guidelines

<http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>

- Issued April 1995
- Three principles:
 - IP is like other property rights
 - IP doesn't necessarily create market power
 - Licensing is procompetitive
 - Integrates complementary resources

Patent Pools – the new view

- Circumspect review, focusing on integration of complements
- Reflecting economic realities of standardized network industries
 - Clear blocking positions
 - Lower search & transaction costs

Key Analytical Issues

- Relationship of the **patents** to each other
 - Complements or substitutes?
 - Robustness of mechanisms
- Relationship of the **members** to each other
 - Horizontal, vertical – or both?
- Degree of exclusivity
 - Is pool license available to all?
 - Alternatives to licensing through pool?
- Potential effect on licensee innovation
 - Development of complementary, non-essential technologies

MPEG-2

<http://www.usdoj.gov/atr/public/busreview/1170.htm>

- Video compression technology
- Originally 9 firms with 27 patents
- Joint licensing agent: MPEG LA
 - Contractually required to give license to all comers
- Licenses for hardware and software
- Members split royalties on per-patent basis

MPEG-2

Key features

- Essential patents
 - Identified by technical expert retained by agent
 - Continuing role for expert
 - Pool patents subject to challenge by members, 3d parties
 - Evaluating applicants' patents
- “Constructive grantback”
 - Licensees effectively must give license to pool members on all “MPEG-2 related patents”
 - Not just essential patents
 - At royalty comparable to pool's per-patent royalty

MPEG-2

The DOJ's Analysis -- 1

- The pool integrates complements
 - Only essential patents are eligible for inclusion in the pool
 - Expert mechanism adequately designed to identify essential patents
 - Royalty allocation method creates financial incentive for members to exclude non-essential patents
 - No significant exclusionary features

MPEG-2

The DOJ's Analysis -- 2

- The pool does not seem likely to inhibit further innovation
 - Members remain free to license outside the standard
 - Licensees are not unreasonably inhibited
 - “Constructive grantback” doesn't unreasonably deter innovation
 - Arguably keeps royalties low, encouraging dissemination
 - A procompetitive price-discrimination device

DVD

- Digital *Versatile* Disc
 - DVD-ROM and DVD-Video
- 2 pools
 - Philips-Sony-Pioneer
 - 3 firms, 95 disc patents, 116 player patents
 - Toshiba-Time Warner
 - 6 firms, 29 disc patents, 22 player patents
- Pool need not include all the essential patents
 - Does it make the world better off?

DVD – Philips-Sony-Pioneer

<http://www.usdoj.gov/atr/public/busreview/2121.htm>

- Philips serves as joint licensor
 - Bilateral agreements with Sony, Pioneer
- Eligible patents:
 - “Necessary (as a practical matter) for compliance”
- Determination of essentiality
 - “Qualified independent expert retained by Philips”

DVD – Philips-Sony-Pioneer

Other Factors

- Members free to offer patents independently of pool
 - Including for non-standard applications
- Royalties allocated on negotiated basis
- No “constructive grantback” on related patents
 - Licensees must contribute essential patents to the pool

DVD – Philips-Sony-Pioneer

The DOJ's Analysis

- Pool combines complements
 - “Flawed” expert mechanism
 - Less independent than MPEG-2 expert
 - Less economic incentive to eject non-essential patents
 - Somewhat subjective essentiality criterion
 - But reasonably likely to limit eligibility to essential patents
 - Written assurances of independence
 - Application of essentiality criterion “scrupulously and independently”
- No other appreciable anticompetitive potential

DVD – Toshiba-Time Warner

<http://www.usdoj.gov/atr/public/busreview/2485.htm>

- Toshiba as joint licensor
 - Multilateral agreement
- Eligible patents:
 - “Technically essential”
 - Patents “for which there is no realistic alternative”
- Determination of essentiality
 - “Outside impartial patent expert or panel”
 - Detailed rules for determination
 - Determination conclusive

DVD – Toshiba-Time Warner

Other Factors

- Members **obligated** to offer patents independently of pool
 - Including for non-standard applications
- Royalties allocated on per-patent basis (adjusted for age)

DVD – Toshiba-Time Warner

The DOJ's Analysis

- Likely to combine complementary patents
 - Expert's independence more robust than in Philips-Sony-Pioneer
 - Economic incentives to eject non-essential patents
- No other appreciable anticompetitive potential

VISX-Summit Technology

<http://www.ftc.gov/os/adjpro/d9286/index.htm>

- Rival technologies
- Infringement litigation
- Settlement: pool formed
 - Mutual exclusivity
 - \$250 per procedure royalty
- FTC sued
- Pool scuttled

What They Stand For

- Complementarity drives the outcome
- Reasonable certainty that the rights are likely to be complements
- Restraints viewed circumspectly
 - Including hard bargains with licensees
 - MPEG-2 “constructive grantback”
- No insistence on competitively optimal result

Unresolved Issues

- Determining essentiality
 - Robustness of mechanism
 - How much can antitrust law realistically ask of pool?
- Acceptability of exclusivity
 - Discrimination against licensees
 - At extreme, exclusivity amounts to a mere cross-license
 - But is that so bad??
- Importance of complementarity?
 - JFTC 3d Generation (3G) wireless telecom letter
 - Licensing program includes rival technologies
 - <http://www.3gpatents.com/press/2000158e.htm#top>