UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION

In the matter of
NEGOTIATED DATA SOLUTIONS, LLC FTC File No. 051-0094

COMMENTS OF STATE ATTORNEYS GENERAL
ON THE FEDERAL TRADE COMMISSION'S PROPOSED CONSENT ORDER
WITH NEGOTIATED DATA SOLUTIONS

The Attorneys General of California, Connecticut, Idaho, Illinois, Iowa, Kansas, Maine, Massachusetts, Mississippi, Oklahoma, Oregon, Rhode Island, Washington and West Virginia ("the States") submit these comments in support of the Federal Trade Commission's proposed consent order regarding *In the Matter of Negotiated Data Solutions* LLC, FTC File 051-0094.

The States have a direct interest in the integrity of Standard Setting Organizations ("SSOs") and the industry standards they promulgate. Such standards hold the potential to increase efficiency and reduce costs for the States' consumers and agencies alike. Yet, these benefits can only be realized if the standard setting process works correctly. Manipulation of the process, such as that presented by N-Data in this case, threaten not only the consumer benefits created by industry standards, but the standard-setting process itself. Accordingly, the States submit these comments in support of the Commission's decision in this case.[1]

1. Because SSO's are an integral part of the economy, the Commission has correctly acted to protect the integrity of the standard-setting process.

SSO's play an essential role in today's economy, offering numerous procompetitive

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[1] The States have done no independent investigation into the matter, but rather, rely on the finding of the FTC as set forth in the Complaint and Analysis.

benefits such as efficiencies, interoperability, improved quality, and in certain cases, improved safety and health[2]. Consumers, including government agencies, are typically direct and indirect beneficiaries of these procompetitive actions. Industry standards often increase interoperability and reduce costs for consumers. Government agencies often incorporate standards into government codes and regulations, benefitting not only from the SSOs' expertise but also from avoiding the costs of duplicative research and testing.

Although SSOs have significant procompetitive potential, they are also "rife with opportunities for anticompetitive activity." *American Society of Mechanical Engineers v. Hydrolevel Corp*., 456 U.S. 566, 571 (1982). Thus, SSOs may facilitate collusion, create significant barriers to entry, and retard innovation. For example, SSO members may agree to exclude a particular competitor or technology that is superior but contrary to the members' pecuniary interests. *ABA Handbook on Antitrust Aspects of Standard Setting*, at 2, 47-49 (2004). Consequently, the Supreme Court has held that conduct of SSOs is subject to antitrust scrutiny. *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492 (1988).

Acknowledging the procompetitive benefits and potential anticompetitive harms of SSOs, the Commission has brought several actions in the recent past against companies that had sought to subvert and undermine the SSO process. In particular, the Commission has acted to prevent "patent ambush" (also referred to as "patent hold up") in the context of an SSO's adoption of a proprietary technology into a standard.

To avoid misuse of the standard-setting process, SSOs typically require *ex ante* disclosure of proprietary technology, as well as assurances that patented technologies essential to

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[2] *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 501, 506-597 (1988). *See also* Mark Lemley, *Intellectual Property Rights and Standard-Setting Organizations*, 90 Calif. L.Rev. 1889, 1896-97 (2002).

a standard will be licensed on reasonable and non-discriminatory ("RAND") terms. A typical patent ambush case involves a company that refuses to comply with one of these requirements and then seeks to exploit its patents once the industry is "locked in" to a standard incorporating that company's intellectual property, typically through extortionate royalty demands and the attendant infringement litigation. Patent "hold up" harms consumers because the increased royalty or switching costs it imposes are often passed on to consumers. Joseph Farrell, John Hayes, Carl Shapiro, and Theresa Sullivan, *Standard Setting, Patents, and Hold Up*, 74 Antitrust L.J. 603, 644-45 (2007). Less obviously, patent hold up potentially harms consumers because it threatens the very existence of SSOs, and the efficiencies they create. As a result, both courts and the Commission have held that patent ambush can violate the antitrust laws. *Broadcom Corp. v Qualcomm, Inc.*, 501 F.3d 297 (3rd Cir.2007); *Hynix Semiconductor v. Rambus Inc*., 2007 U.S. Dist. Lexis 84697 (N.D.Cal.2007); *FTC v. Rambus*, FTC Docket No. 9302 (2006), *rev'd, Rambus v. F.T.C.*, 2008 U.S. App. LEXIS 8662 (D.C.Cir. 2008); *FTC v. Dell*, 121 F.T.C. 616 (1996).

2. Intentional, opportunistic conduct that undermines the procompetitive purposes and effects of standard-setting harms competition and consumers.

Deception in the standard-setting process can cause significant harm, not only to SSO participants, but to consumers as well. Harm is likely to occur when (i) the deception relates to defendants' proprietary rights in certain technologies; (ii) the SSO is justifiably unaware of the defendant's propriety rights (in cases where disclosure was made), or the defendant makes certain assurances regarding RAND licensing of its rights; (iii) the SSO is justified in relying on defendants disclosures (or non-disclosures) and/or licensing assertions; (iv) the defendant's proprietary technology is adopted into a standard and is an essential part of the standard; (vi) the

standard becomes commercially successful and is incorporated into a sufficient number of end products to make switching to an alternative technology difficult or impossible; and (vii) after the standard becomes commercially successful, the defendant either discloses and seeks to enforce its proprietary rights, or reneges on its RAND licensing commitments. *Broadcom Corp. v. Qualcomm, Inc.*, 501 F.3d 297 (3rd Cir.2007); *FTC v. Rambus*, FTC Docket No. 9302 (2006), *rev'd, Rambus v. F.T.C.*, 2008 U.S. App. LEXIS 8662 (D.C.Cir. 2008); *FTC v. Unocal*, FTC Docket No. 9305 (2003); *FTC v. Dell*, 121 F.T.C. 616 (1996).

Although most of the recent antitrust cases involving SSOs have involved deceptive conduct, deception is not the only type of conduct that may be anticompetitive. Indeed, the Supreme Court has held that intentional, opportunistic conduct that subverts the SSO process, even if neither deceptive nor expressly prohibited by SSO rules and policies, may be anticompetitive. Thus, in *Allied Tube*, the Court upheld a jury verdict of antitrust liability against producers of steel conduits who "rigged" the decision-making process by recruiting new members, thus successfully manipulating the SSO for their own competitive advantage. *Allied Tube*, 817 F.2d 938 (2nd Cir. 1987), *aff'd*, 486 U.S. 492 (1988). Similarly, in *Hydrolevel*, the dominant manufacturer of low-water fuel cutoffs, a safety device for heating boilers, abused its position as a member of an SSO to conspire with other members and issue an SSO opinion finding a competitor's product to be unsafe. The Court affirmed a jury verdict of antitrust liability. *Hydrolevel*, 635 F.2d 118 (2nd Cir. 1980), *aff'd*, 456 U.S. 556 (1982). Thus, anticompetitive conduct in the standard setting context may take a variety of forms.

3. N-Data's decision to renege on its predecessor's promises subverts the standard setting process and is likely to have anticompetitive effects. The Commission's Proposed Consent Order properly addresses these anticompetitive effects under Section 5 of the FTC Act.

In this case, the inventor and predecessor to the relevant patents at issue, National Semiconductor Incorporation ("National"), competed to incorporate its patented technology into the relevant standard by offering a flat licensing fee of $1,000. Once the industry was locked in to a standard incorporating this technology, N-Data reneged on the promise and began to, in effect, extort money from market participants. Analysis at 3**.** No efficiencies justified this conduct. Moreover, it was "coercive" and had an "adverse effect on prices for autonegotiation technology." Accordingly, the Commission held the conduct to be an unfair method of competition in violation of Section 5 of the FTC Act[3]. The Commission also held that N-Data's conduct was an unfair act or practice in violation of the FTC Act because it caused "substantial consumer injury" that consumers could not reasonably avoid, and that had no countervailing competitive benefits. Analysis at 7.

The Commission's remedy for this violation is reasonable and practical: Requiring N-Data to stand by National's promised licensing terms. To remedy the violation, the Proposed Consent Order prohibits N-Data from enforcing the patents at issue unless it first offers a license

[3] Analysis at 5-6. The majority and dissenting opinions note that the Commission chose not to base its analysis in this case on Section 2 of the Sherman Act. One of the concerns underlying this decision appears to be the belief that reliance on the FTC Act reduces the likelihood of follow-on private actions. *See* Dissenting Statement of Commissioner Kovacic. The States take no position on this issue, other than to note, as Commissioner Kovacic pointed out in his dissent, that Section 5 analysis may not necessarily create less follow on litigation than Section 2 analysis. *Id.* at 2. For example, Section 2 of the Sherman Act provides a nationwide private right of action, but denies standing to indirect purchasers. Although Section 5 does not provide a nationwide private right of action, most states have mini-FTC Acts or similar consumer protection statutes, many of which permit a private right of action, and few of which deny standing to indirect purchasers.

on the terms promised by National.[4]

The States approve the Commission's resolution of this matter. If permitted to stand, NData's conduct would likely harm consumers by either increasing prices or requiring consumers to purchase non-interoperable end products using competing technologies. More generally, conduct like N-Data's threatens the very viability of SSOs as a means of cooperative development. If members of an SSO cannot rely on other members' disclosures and commitments, SSOs along with their procompetitive consumer benefits, may cease to exist. Consequently, the States believe the Proposed Consent Order should be finalized.

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Respectfully submitted,

Edmund G. Brown, Jr.
Attorney General of California
California Department of Justice
1300 I Street, Suite 1740
Sacramento, CA 95814
(916) 324-5437

Richard Blumenthal
Attorney General of Connecticut
Office of the Attorney General
55 Elm Street
Hartford, CT 06141-0120
(860) 808-5324

Lawrence Wasden
Attorney General of Idaho
Office of the Attorney General
700 W. State Street, 2nd Floor
Boise, ID 83720
(208) 334-2400

Lisa Madigan
Attorney General of Illinois
Office of the Attorney General
James R. Thompson Center
100 West Randolph Street
Chicago, IL 60601
(312) 814-3000

[4] Recognizing that some firms may inadvertently fail to accept the offer in a timely manner, thereby disadvantaging N-Data, the Proposed Order permits N-Data to charge $35,000 at the time it files an infringement action, so long as the action is preceded by a previous offer on the original terms, and at least 120 days have lapse since the offer was made

Tom Miller
Attorney General of Iowa
Office of the Attorney General
Hoover State Office Building
1305 East Walnut
Des Moines, IA 50319
(515) 281-3053

Stephen Six
Attorney General of Kansas
Office of the Attorney General
120 S.W. 10th Avenue, 2nd Floor
Topeka, KS 66612-1597
(785) 296-2215

Steven Rowe
Attorney General of Maine
Office of the Attorney General
State House Station Six
Augusta, ME 04333
(207) 626-8800

Martha Coakley
Attorney General of Massachusetts
Office of the Attorney General
One Ashburton Place
Boston, MA 02108-1698
(617) 727-2200

Jim Hood
Attorney General of Mississippi
Department of Justice
Post Office Box 220
Jackson, MS 39205-0220
(601) 359-3692

W.A. Drew Edmondson
Attorney General of Oklahoma
Office of the Attorney General
State Capitol, Room 112
2300 North Lincoln Boulevard
Oklahoma City, OK 73105
(405) 521-3921

Hardy Myers
Attorney General of Oregon
Office of the Attorney General
Justice Building
1162 Court Street NE
Salem, OR 97301
(503) 378-6002

Patrick Lynch
Attorney General of Rhode Island
Office of the Attorney General
150 South Main Street
Providence, RI 02903
(401) 274-4400

Rob McKenna
Attorney General of Washington
Office of the Attorney General
900 4th Street, Suite 2000
Olympia, WA 98504-0100
(360) 753-6200

Darrell V. McGraw, Jr.
Attorney General of West Virginia
Office of the Attorney General
State Capitol
1900 Kanawha Boulevard East
Charleston, WV 25305
(304) 558-2021