COMMENT OF THE GLOBAL ANTITRUST INSTITUTE, GEORGE MASON UNIVERSITY SCHOOL OF LAW, ON THE STATE ADMINISTRATION FOR INDUSTRY AND COMMERCE ANTI-MONOPOLY GUIDELINES ON THE ABUSE OF INTELLECTUAL PROPERTY RIGHTS

January 11, 2016

This comment is submitted in response to the State Administration for Industry and Commerce's (SAIC's) Anti-Monopoly Guidelines on Abuse of Intellectual Property Rights (Draft Guidelines). We appreciate the opportunity to comment and commend the SAIC for its transparency. We submit this comment based upon our extensive experience and expertise in antitrust law and economics generally, and specifically with respect to the intersection of intellectual property and antitrust.[1]

INTRODUCTION

We commend the SAIC for its general approach, as set forth in Chapter I on General Provisions, of recognizing explicitly an intellectual property right (IPR) holder's core right to exclude and condemning as an Anti-Monopoly Law (AML) violation only those acts that (1) breach "the scope and purpose" of an IPR under the applicable laws and regulations granting the right, and (2) eliminate or restrict competition. We are concerned, however, that the Draft Guidelines fail to incorporate throughout the well-accepted methodological principle that, when assessing the possible competitive effects of the use of IPRs, agencies should compare the competitive impact of the IPR use against what would have happened in the "but for" world in the absence of a license. This important analytical approach, which has been used by the U.S. antitrust agencies for the last 20 years, is missing throughout the Draft Guidelines.

We are also concerned that the Draft Guidelines create a number of presumptions that certain conduct (such as entering into exclusive grantbacks, tying and bundling arrangements, or pooling arrangements, charging for expired or invalid patents, and prohibiting a licensee from challenging the validity of its IPR) will, or is likely to, eliminate or restrict competition. We respectfully urge the elimination of such presumptions and recommend that the SAIC instead adopt an effects-based approach in which licensing restraints are condemned only when any anticompetitive harm they may cause outweighs any procompetitive benefits they create. This approach would benefit Chinese consumers because presumptions of competitive harm are likely

[1] The Global Antitrust Institute (GAI) at George Mason University is a leading international platform for research and education that focuses on the legal and economic analysis of key antitrust issues confronting competition agencies and courts around the world. Professor of Law Joshua D. Wright, Ph.D. (economics), is the Executive Director of the GAI and a former U.S. Federal Trade Commissioner. Koren W. Wong-Ervin is the Director of the GAI and former Counsel for Intellectual Property and International Antitrust at the U.S. Federal Trade Commission. Professor of Law Douglas H. Ginsburg is a Senior Judge, United States Court of Appeals for the District of Columbia Circuit, Chairman of the GAI's International Board of Advisors, and a former Assistant Attorney General in charge of the Antitrust Division of the U.S. Department of Justice. Professor of Law Bruce H. Kobayashi, Ph.D. (economics), is a GAI Senior Scholar and Founding Director.

to have a chilling effect on potentially procompetitive conduct by subjecting entities to a higher likelihood of liability under the AML. Adopting an approach that incorporates these revisions is likely to best serve competition and consumers, as well as China's goal of becoming an innovation society.

THE ECONOMICS OF INNOVATION

Economic literature shows that IPRs—a central feature of which is the right to exclude—incentivize the creation of inventions, ideas, and original works.[2] They also facilitate the sale and licensing of intellectual property (IP) by defining the scope of property right protection and lowering transaction costs, and they produce incentives to develop alternative technologies as well as improvements and other derivative uses.

The incentive function of IP is illustrated by considering the sale of an invention in the absence of enforceable IPRs. The sale of an invention requires disclosure to the potential buyer. In the absence of enforceable IPRs, the potential buyer—now with knowledge of the invention—has no incentive to purchase or license the invention. This possibility deters the seller from disclosing the invention in the first place. Enforceable property rights solve this problem by allowing the seller to disclose the invention without fear that it will be lawfully appropriated without compensation. The inventor can anticipate the ability to appropriate the returns from investment in producing the invention, which serves as an incentive to invest in producing and to disclose the invention in the first place.

The economic literature also focuses on the related issue of the optimal tradeoff between these incentives and the ability to use the invention.[3] Because inventions and works protected by IPRs are non-rivalrous, one firm using a specific IPR does not diminish the ability of another firm to use the same IPR. Also, the cost of having another firm use an existing IPR is effectively zero. As a consequence, from a static welfare perspective, it is desirable to disseminate IPRs to every firm (or consumer) that has a positive valuation for the IPR. Of course, doing so would create a strong disincentive to innovate in the first place, to the great detriment of dynamic efficiency, which refers to the gains that result from entirely new ways of doing business. While static efficiency may increase consumer welfare in the short run, economics teaches us that dynamic efficiency, including societal gains from innovation, are an even greater driver of consumer welfare.[4]

After the investments and competitive effort required to spur breakthrough inventions

---

[2] *See* Bruce H. Kobayashi & Joshua D. Wright, *Intellectual Property and Standard Setting* in the ABA HANDBOOK ON THE ANTITRUST ASPECTS OF STANDARD SETTING 1, 2 (2010) (citing William M. Landes & Richard A. Posner, THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW (2003)) [hereinafter Kobayashi & Wright]; Henry E. Smith, *Intellectual Property as Property: Delineating Entitlements in Information*," 116 YALE L.J. 1742 (2007).

[3] Kobayashi & Wright, *supra* note 2.

[4] Robert Solow won the Nobel Prize in economics for demonstrating that gains in wealth are due primarily to innovation—not to marginal improvements in the efficiency of what already exists. *See* Press Release (Oct. 21, 1987), http://www.nobelprize.org/nobel_prizes/economic-sciences/laureates/1987/press.html.

have been made and proven successful, it can be tempting to carve up the benefits and distribute them throughout the economy. Doing so, however, would harm competition, innovation, and consumers. If the government is too willing to step in and appropriate the gains from innovation and dynamic competition, then potential innovators anticipating such interventions will have weak incentives to risk investment in new inventions. Likewise, if the laws governing abuse of IPRs is uncertain or unpredictable (which they would be if the vague prohibition of "unfairly high pricing" is applied to IPRs), potential innovators will also have weak incentives to innovate.

RECOMMENDATIONS ON SPECIFIC PROVISIONS

I. Chapter IV.18 – Exclusive Grantback License

Chapter IV.18 appears to create a presumption of illegality for exclusive grantbacks, stating that such licenses are "usually not an essential factor to increase the potential efficiency." We respectfully urge that this provision be revised to explicitly recognize that exclusive grantbacks may be procompetitive and that the SAIC will analyze them under an effects-based approach in which licensing restraints are condemned only when any anticompetitive harm they may cause outweighs any procompetitive benefits they create.

Grantbacks, including exclusive grantbacks, may provide substantial procompetitive benefits because they may facilitate the integration of complementary technologies and provide incentives both for innovation in the first place and for subsequent licensing of the results of that innovation.[5] Grantbacks also provide a means for the licensee and the licensor to share risks and to reward the licensor for possible further innovations based upon or informed by the licensed technology.[6]

While the U.S. antitrust agencies recognize that non-exclusive grantbacks are "less likely to have anticompetitive effects," they nevertheless analyze both exclusive and non-exclusive grantbacks under the "rule of reason," which is an effects-based approach. As such, "[i]f the Agencies determine that a particular grantback provision is likely to reduce significantly licensees' incentives to invest in improving the licensed technology, the Agencies will consider the extent to which the grantback provision has offsetting procompetitive effects," such as (1) increasing licensors' incentives to innovate in the first place, (2) promoting dissemination of licensee's improvements to the licensed technology, (3) increasing the licensors' incentives to disseminate the licensed technology, or (4) otherwise increasing competition and output in a relevant technology or innovation market.[7]

---

[5] *See, e.g.,* DEP'T OF JUSTICE & FED. TRADE COMM'N., ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY §§ 5.5 and 5.6 (1995), http://www.justice.gov/atr/public/guidelines/0558.pdf [hereinafter DOJ-FTC IP GUIDELINES].

[6] *See id.* § 5.6.

[7] *Id.*

II. Chapter V -- IPR-Related Abuse of Market Dominance

Chapter V.26. – Refusal to License IPRs

Chapter V.26 governs refusals to license. We commend the SAIC for recognizing that the "[r]efusal to grant a license represents one way in which an IPR owner exercises its IPR," and that the AML agencies "generally would not impose an obligation on the IPR owner to enter into transactions with any competitors or counterparties." This is consistent with the approach taken by the U.S. antitrust agencies, which have stated that "[a]ntitrust liability for mere unilateral, unconditional refusals to license will not play a meaningful part" in their enforcement efforts.[8] This approach recognizes that antitrust liability for refusals to license would impair an IPR holder's core right to exclude, which is likely to lessen the incentive to innovate. In addition, "liability for refusals to license competitors would compel firms to reach out and affirmatively assist their rival, a result that is 'in some tension with the underlying purpose of antitrust law.'"[9]

However, Chapter V.26 would impose possible AML liability for an IPR holder's failure to license an IPR that constitutes a "necessity in production and operating activities" and creates a presumption that such conduct "generally has the effect of eliminating or restricting competition" when the IPR cannot "be reasonably replaced in the relevant market." For the reasons set forth below, we respectfully urge that this provision be omitted in its entirety or, at the very least, be revised to eliminate any presumption of illegality in favor of an effects-based approach.

First, although a firm's competitors may desire to use a particular technology in their own products, there are few situations, if any, in which access to a particular IPR is necessary to compete in a market. Indeed, those who advocate forced sharing of an "essential" facility (or "necessary" technology) often have underestimated the ability of a determined rival to compete around the facility, with resulting benefits to consumers. This is particularly true with respect to fast moving technologies, where technological and market developments can present multiple opportunities to work around a competitor's IP, and it is easier to work around an IPR than it is to work around a physical structure. Recognizing these concerns, the U.S. Supreme Court has made it clear that it will treat so-called "essential facilities" claims with great skepticism, stating that courts should be very cautious in recognizing exceptions to the general rule that even monopolists may choose with whom they deal.[10]

Second, the U.S. approach recognizes that potential inventors may be less likely to undertake the research and development that lead to an invention if the inventor's reward for its efforts is reduced by having to share its patent. Conversely, if businesses know they can easily gain access to the patents of other firms, then they have less incentive to innovate and more

---

[8] DEP'T OF JUSTICE & FED. TRADE COMM'N., *Antitrust Enforcement and Intellectual Property Rights: Promoting Competition and Innovation* at 6 (April 2007), http://www.ftc.gov/reports/innovation/P040101PromotingInnovationandCompetitionrpt0704.pdf.

[9] *Id.* (quoting Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407-08 (2004) (setting forth three sources of that tension)).

[10] *See Trinko*, 540 U.S. at 408.

incentive instead to free-ride on the risky and expensive research of others.[11] Requiring businesses to grant licenses to competitors wishing to use a patented invention is likely to result in less innovation, which will harm consumers in the long run.

Lastly, should the SAIC retain this provision, we urge that it at least be revised to explicitly acknowledge that a patentee's ability to license may be limited because the patent has been or may be exhausted. Under the patent exhaustion doctrine, once there has been an authorized sale of a patented item, that sale "confers on the purchaser, or any subsequent owner, 'the right to use [or] sell' the thing as he sees fit."[12] Patent exhaustion eliminates the legal restrictions on what authorized acquirers "can do with an article embodying or containing an invention" whose initial sale (or comparable transfer) the patentee authorized.[13] Given the patent exhaustion doctrine, the licensor may chose not to license its IPR to certain persons or at certain levels of the distribution chain.

Chapter V.27 – IPR-Related Tie-In Sales

Chapter V.27 creates a presumption that tie-in sales that meet the following two conditions "generally" have the effect of eliminating or restricting competition: (1) "compulsory bundling or combination of sales of different commodities in violation of trade usages, spending habits, or other practices or in disregard of the commodities' functions; and (2) extension of the undertaking's dominant position in the tying product market to the tied product market as a result of the tie-in sale, resulting in the elimination or restriction of competition from other undertakings in the tying product market or tied product market." We respectfully urge that this provision be revised to eliminate the presumption and to state explicitly that the SAIC will analyze tying under an effects-based approach in which licensing restraints are condemned only when any anticompetitive harm they cause outweighs any procompetitive benefits they create.

Tying and bundling, like other licensing restraints, are generally procompetitive because they may facilitate the integration of complementary technologies, promote the dissemination of a technology, and reduce transaction costs.[14] Bundling, for example, may be efficiency enhancing when multiple licenses are needed to use a single item of IP. Many economists believe that, in general, tying and bundling are much more likely to be procompetitive than anticompetitive.[15] As such, the U.S. antitrust agencies have stated that, "[i]n the exercise of their

---

[11] *See id.*

[12] *Bowman v. Monsanto Co.*, 133 S. Ct. 1761, 1766 (2013) (quoting *United States v. Univis Lens Co.*, 316 U.S. 241, 249-50 (1942)).

[13] *Bowman*, 133 S. Ct. at 1766 & n.2.

[14] *See, e.g.,* DOJ-FTC IP GUIDELINES, *supra* note 5, §§5.5 and 5.6.

[15] *See, e.g.*, Alden F. Abbott & Joshua D. Wright, *Antitrust Analysis of Tying Arrangements and Exclusive Dealing* at 10 (2009) (citing David Evans & Michael Salinger, *Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law*, 22 YALE J. ON REG. 37 (2005)), http://www.law.gmu.edu/assets/files/publications/working_papers/08-37%20Antitrust%20Analysis%20of%20Tying.pdf; *see also generally* Anne Layne-Farrar & Michael A. Salinger, *Bundling of RAND-Committed Patents* (June 2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2585528; Bruce H. Kobayashi, *Does Economics*

prosecutorial discretion, [they] will consider both the anticompetitive effects and the efficiencies attributable to a tie-in."[16] The U.S. antitrust agencies use the same effects-based approach to evaluate bundled and package sales.

Chapter V.28 – Additional Unreasonable Trading Conditions in Connection with IPRs

Chapter V.28 appears to create *per se* liability for the following conduct if undertaken by an IPR holder "without due cause": (1) "requiring its counterparty to grant technological improvements exclusively back to it; (2) prohibiting its counterparty from questioning the validity of its IPR; (3) "restricting its counterparty from utilizing competitive commodities or technologies after the licensing agreement expires when such utilization does not violate any IPR"; (4) "continuing to exercise an IPR when its term of protection has expired or when it has been deemed to be invalid"; (5) "prohibiting the counterparty from entering into a transaction with a third party"; and (6) "imposing other unreasonably restrictive conditions on the counterparty." We respectfully urge that this provision be revised to abandon the *per* se approach in favor of an effects-based approach in which licensing restraints are condemned only when any anticompetitive harm they cause outweighs any procompetitive benefits they create. In addition, for the reasons set forth below, we strongly urge that the SAIC not base AML violations on charging for expired or invalid patents or entering into agreements that prohibit licensees from challenging validity.

As explained in Section I, above, grantbacks, including exclusive grantbacks, like other licensing restraints, are generally procompetitive because they facilitate the integration of complementary technologies. Grantbacks also provide a means for the licensee and the licensor to share risks and to reward the licensor for possible further innovations based upon or informed by the licensed technology. Finally, the prospect of a grantback is an incentive both for innovation in the first place and for the subsequent licensing of the results of that innovation.[17] Exclusive grantbacks, like other licensing restraints, should be analyzed case by case, under an effects-based approach.

With respect to charging for expired patents, it would be impractical, if not impossible, for portfolio owners to constantly renegotiate licenses (or provide updated patent lists) every time an IPR expires or new IPR is added to the portfolio. Portfolios include patents with a variety of expiration dates, which the parties to the license take into account when negotiating a price.

Similarly, as a practical matter, particularly when large portfolios are involved, an implementer that insists on challenging validity on a patent-by-patent basis around the world may be engaged in bad-faith licensing delay, or holdout. Nevertheless, implementers have the opportunity to challenge the validity of an IPR at any moment from the time the patent office grants the patent at issue until the time it executes a license with a no-challenge clause. A no-

---

Provide a Reliable Guide to Regulating Commodity Bundling by Firms? A Survey of the Economic Literature, 1 J. COMPETITION L. & ECON. 4, 707 (2005).

[16] DOJ-FTC IP GUIDELINES, *supra* note 5, § 5.3.

[17] *See* DOJ-FTC IP GUIDELINES, *supra* note 5, § 5.6.

challenge clause constrains the implementer's ability to challenge the validity of an IPR only *after* it has already executed a license agreement. When a licensor and a licensee negotiate a license for a large IPR portfolio, both parties understand that some of the hundreds or thousands of patents in the portfolio may be invalid. The parties do not invest extensive resources in identifying those invalid patents, which would make the transaction prohibitively costly. Instead, the parties assess generally the value of the licensed portfolio and determine a royalty that accounts for the possibility that some of the portfolio's patents may be invalid. In addition, IPR holders typically remove obsolete patents from the portfolio and add new patents that have become relevant since the parties executed the license agreement. This industry practice of portfolio "rebalancing" further reduces the risk that the presence of a few invalid patents would impose any significant cost on the licensee. Encouraging a licensee to challenge the validity of individual licensed patents invites opportunistic litigation by the licensee so as to delay paying the IPR holder the agreed-upon royalty for the use of the many more valid patents in its licensed portfolio. Thwarting an IPR holder's ability to receive prompt compensation for its innovative contribution lessens the IPR holder's incentive to invest in innovation, which in turn imposes significant harm on consumers.[18]

III. Chapter VII – Antitrust Analysis of Certain Specific IP-Related Acts

Chapter VII.29 – General Analysis of Exercise of IPRs in Setting and Implementing Standards

Chapter VII.29 governs conduct related to standard-essential patents (SEPs). We commend the SAIC for recognizing that SEPs do not necessarily confer market power. We respectfully urge that this provision be revised to specify that the analysis will focus on the ability of the SEP holder to profitably maintain prices above or output below competitive levels for a significant period of time, and the existence of actual or potential close substitutes that prevent the exercise of market power. We also respectfully urge the SAIC to clarify that Chapter VII.29-30 apply only to SEPs on which the patent holder has made a *voluntary* commitment to a standard-setting organization (SSO) to license on fair, reasonable, and non-discriminatory (FRAND) terms (commonly referred to as "FRAND-assured SEPs").

Chapter VII.29 also provides for possible AML liability for failure to disclose essential patents. We respectfully urge that this provision be revised to specify that liability will be imposed only when there is proof of the following six elements: (1) the patent holder or applicant is an active voting participant in a standard-setting organization (SSO); (2) the patent holder knows or should know that its patent or pending patent (patent application) may be incorporated into the relevant standard; (3) the patent holder or applicant deliberately conceals information about that patent from the SSO in violation of the SSO's policies on written disclosures; (4) after adoption of the standard, the patent holder or applicant asserts its standard-essential patents against implementers of mandatory portions of the standard; (5) but for the patent holder's or applicant's failure to disclose, a different technology would have been incorporated into the

[18] *See* J. Gregory Sidak, *Evading Portfolio Royalties For Standard-Essential Patents Through Validity Challenges* (2015), https://www.criterioneconomics.com/docs/evading-portfolio-royalties-for-seps.pdf.

standard; and (6) the patent holder's or applicant's conduct causes or is likely to cause an adverse effect upon competition in the relevant market.[19]

The fifth requirement is particularly important. If the technology would have been adopted regardless whether the SEP holder had made the disclosure, then the SEP holder did not prevent or lessen competition in a market. As the U.S. Court of Appeals for the D.C. Circuit explained in *Rambus Inc. v. Federal Trade Commission*, if the SSO would have standardized the technology *even if* the SEP holder had disclosed its intellectual property, then the SSO would have lost

> only an opportunity to secure a [F]RAND commitment from [the SEP holder]. But loss of such a commitment is not a harm to competition from alternative technologies in the relevant markets. . . . Indeed, had [the SSO] limited [the SEP holder] to reasonable royalties and required it to provide licenses on a nondiscriminatory basis, we would expect to see *less* competition from alternative technologies, not more; high prices and constrained output tend to attract competitors, not to repel them.[20]

Chapter VII.29 also provides the following examples of when a failure to disclose may "cause adverse impact[s] on competition and innovation": "the patentee refuses, without justifiable reason, to grant a license to any person who uses such standard to exploit its patent on reasonable terms and conditions; or such patentee discriminates, without justifiable reason, the users of such standard with equal conditions, in terms of licensing conditions such as licensing price." We note that discriminatory licensing can serve legitimate, procompetitive ends and enhance consumer welfare.[21] Moreover, whether an SEP holder violates the "non-discriminatory or ND" element of FRAND is wholly dependent on the individual SSO Intellectual Property Rights (IPR) policy at issue, and these policies vary widely.[22] For example, some SSO IPR policies define a FRAND commitment as a commitment to license "all comers," while others limit the commitment to specific levels of the distribution chain (e.g., end-user products as opposed to component parts, such as chipsets).

---

[19] *See, e.g.*, Rambus Inc. v. Federal Trade Commission, 522 F.3d 456, 464-67 (D.C. Cir. 2008); *see also* Bruce H. Kobayashi & Joshua D. Wright, *The Limits of Antitrust and Patent Holdup: A Reply to Cary, et al.,* 78 ANTITRUST L.J. 505 (2012) [hereinafter Kobayashi & Wright].

[20] *Rambus Inc.*, 522 F.3d 456 at 466 (emphasis in original).

[21] *See, e.g.*, Anne Layne-Farrar, *Nondiscriminatory Pricing: Is Standard Setting Different?*, 6 J. COMPETITION L. & ECON. 4, 811, 811, 814-17 (Dec. 2010) (the existing literature on price discrimination in traditional markets for goods and services and on licensing intellectual property establishes that "price discrimination is not necessarily harmful, and in some cases can even increase consumer welfare; most IP licensing is characterized by 'discrimination' in that rates and terms tend to differ across licensees; proof of market power must remain the first step in any inquiry on allegations of anticompetitive IP licensing discrimination; and as of yet, no widely applicable benchmarks or rules for distinguishing harmful from beneficial or non-harmful licensing discrimination have emerged, meaning that a careful, quantitative effects-based analysis remains the best approach.") [hereinafter Layne-Farrar].

[22] *See* Joanna Tsai & Joshua D. Wright, *Standard Setting, Intellectual Property Rights, and the Role of Antitrust in Regulating Incomplete Contracts*, 80 ANTITRUST L.J. 157 (2015).

Price discrimination in particular helps a firm with fixed costs to recover its outlays and is sometimes necessary for a firm to recover those outlays.[23] Indeed, an important aspect to consider in evaluating discrimination in licensing as compared to price discrimination for physical goods is the nature of IP development. The innovation process typically involves large upfront investments in research and development yet very low marginal costs at the production stage. Economists have observed that price discrimination can be an important mechanism for recovering fixed costs under these circumstances.[24]

Price discrimination can improve efficiency, grow markets, intensify competition, and enhance consumer welfare. "For example, it can enable price-sensitive consumers to be served when they otherwise would be priced out of the market if uniform pricing were mandated."[25] When there are two distinct customer groups, one that is highly price sensitive and another that is not, without price discrimination firms may price relatively high for the latter group to maximize their profits. As a result, the first group will be foreclosed from the market. And, "for certain market structures, price discrimination can also lead to lower overall prices for consumers in comparison with uniform prices."[26]

Similarly, discriminatory refusals to license or licensing to different parties on different terms may serve legitimate, procompetitive ends. For example, a business may grant licenses to some, but not all, interested potential licensees in order to ensure that licensees have a greater incentive to promote the licensor's technology. Alternatively, in order to maximize its incomes from the patent, a business may require higher royalties from a company that has lower sales volume or offer lower royalties to a licensee that can offer valuable consideration in trade, such as a cross-license of its IP, which may be netted against the price of a license.

In the United States, nearly all concern over potentially harmful discriminatory licensing has centered on the practices of vertically integrated firms that both hold patents and practice them in a downstream market. This is because a nonintegrated patent holder, with no downstream operations, has less to gain by discriminating among licensees with whom it does

---

[23] Layne-Farrar, *supra* note 21 at 827 (citing William J. Baumol & Daniel G. Swanson, *The New Economy and Ubiquitous Competitive Price Discrimination: Identifying Defensible Criteria of Market Power, Symposium on Competitive Price Discrimination*, 70 ANTITRUST L.J. 661 (2003)).

[24] Layne-Farrar, *supra* note 21 at 827 & n.53-54 (collecting cites).

[25] *Id.* at 815 (citing Benjamin Klein & John Wiley, Jr., *Competitive Price Discrimination As an Antitrust Justification for Intellectual Property Refusals to Deal*, 70 ANTITRUST L.J. 599 (2003); Richard Schmalensee, *Output and Welfare Implications of Monopolistic Third-Degree Price Discrimination*, 71 AM. ECON. REV. 242 (1981); Hal R. Varian, *Price Discrimination*, in HANDBOOK OF INDUSTRIAL ORGANIZATION 597 (Richard Schmalensee & Robert D. Willig eds., North-Holland 1989) (surveying price discrimination theory and practices); Lars A. Stole, *Price Discrimination and Competition*, in 3 HANDBOOK OF INDUSTRIAL ORGANIZATION 2223 (Mark Armstrong & Robert Porter eds., Univ. of Chicago 2007)).

[26] Layne-Farrar, *supra* note 21 at 816 (citing Jacques F. Thisse & Xavier Vives, *On the Strategic Choice of Spatial Price Policy*, 78 AM. ECON. REV. M. 122 (1988); D. Fudenberg & J. Tirole, *Customer Poaching and Brand Switching*, 31 RAND J. ECON. 634 (2000)).

not compete.[27] Nonintegrated firms will have incentive to engage in anticompetitive licensing discrimination only if it increases their total royalty revenues, but often it is increased downstream competition that maximizes upstream patentee's royalty earnings.[28] If the patent holder is not vertically integrated then the analysis of allegations of discriminatory licensing should be scrutinized even more rigorously because the circumstances under which an upstream patent holder would have an incentive to disadvantage one downstream licensee over another are narrower.[29] Lastly, the possibility of market expansion and other efficiencies, including the coverage of research and development investments, indicates the need for a cautious approach to assessing discrimination in licensing—including involving SEPs—even when vertically integrated firms are involved.

Chapter VII.30 – AML Provisions on Injunctive Relief in Relation to SEPs

Chapter VII.30 provides an SEP holder that applies for injunctive relief "may" be found to violate the AML by engaging in any of the following acts:

> (a) the SEP owner directly applies for the injunction without first giving any warning to the user of standard, specifying the infringement committed by such user;
>
> (b) the SEP owner directly applies for the injunction without considering, or extending a written offer of license to the user of standard upon, the intention expressed by the user of standard to negotiate on a FRAND license;
>
> (c) where the user of standard expressly states its willingness to accept a ruling based on the FRAND principle made by a court or the arbitration body agreed by the parties, the SEP owner still applies for the injunction; or
>
> (d) other events decided by the AML law enforcement agency of the State Council.

Chapter VII.30 also provides a safe harbor from AML liability when the SEP holder "produces evidence" that the accused infringer (1) "clearly lacks the good faith to negotiate," (2) "fails to actively engage in the negotiation in accordance with commercial practice or in good faith," (3) "deliberately protracts the negotiation process," (4) "refuses to pay royalties," or (5) is unable to pay royalties and damages."

For the reasons set forth below, we strongly urge that this provision be deleted in its entirety, and that the SAIC not impose an AML sanction for merely seeking an injunction. There is no empirical evidence to support the concerns that injunctive relief results in harm to innovation or to consumers, and the burden of establishing any harm from a counterparty's having sought an injunction should rightly be on those advocating this fundamental policy shift.

---

[27] *See, e.g.*, Herbert Hovenkamp, Mark D. Janis, & Mark A. Lemely, *Unilateral Refusals to License in the US*, 2 J. COMPETITION L. & ECON. 1, 16 (Mar. 2006).

[28] Layne-Farrar, *supra* note 21 at 825.

[29] *Id.* at 828.

In addition, reverse holdup and holdout[30] are both possibilities and therefore there are likely to be detrimental consequences to disrupting the carefully balanced FRAND ecosystem by creating an AML sanction for the seeking of injunctive relief.[31] Indeed, creating an AML sanction for the seeking of injunctive relief significantly alters the critical balance between the interests of SEP holders and the interests of implementers. As the European Court of Justice (ECJ) recognized in *Huawei v. ZTE*, it is essential "to ensure a fair balance between the interests concerned."[32] In addition, imposing an AML sanction is likely to reduce incentives to innovate and deter SEP holders from participating in standard setting, thereby depriving consumers of the substantial procompetitive benefits of standardized technologies.[33] Lastly, injunctions issue only upon a court order. This critical gatekeeper minimizes the risk of any potential harm. As such, the mere seeking of injunctive relief alone does not monopolize the market because courts independently assess whether an injunction is warranted, taking into consideration whether the public interest would be disserved by an injunction.[34] As for the notion that the mere threat of an injunction may cause harm, the *in terrorem* (or fear from threat) effect of filing for an injunction depends on the likelihood of it being granted.

In the alternative, should the SAIC decide to adopt an AML sanction for seeking injunctive relief—which we strongly urge it not to do—at the very least, it should limit liability to situations in which there is proof that a FRAND-assured SEP holder has engaged in patent holdup, i.e., that the patent holder used the threat of injunctive relief to demand supra-

---

[30] Holdup requires lock-in, and standard-implementing companies with asset-specific investments can be locked in to the technologies defining the standard. On the other hand, innovators that are contributing to an SSO can also be locked-in if their technologies have a market only within the standard. Thus, incentives to engage in holdup run in both directions. There is also the possibility of holdout. While reverse holdup refers to the situation when licensees use their leverage to obtain rates and terms below FRAND, holdout refers to licensees either refusing to take a FRAND license or delaying doing so.

[31] *See, e.g.*, Luke Froeb & Mikhael Shor, *Innovators, Implementers, and Two-Sided Hold-Up,* ANTITRUST SOURCE at 3 (Aug. 2015), http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/aug15_froeb_7_21f.authcheckdam.pdf (explaining that the curtailing of injunctive relief serves "to shift bargaining power and profits from innovators to implementers," which "weakens the value of patents and can significantly reduce the incentive to innovate"); Bernhard Ganglmair, Luke M. Froeb & Gregory J. Werden, *Patent Hold Up and Antitrust: How a Well-Intentioned Rule Could Retard Innovation*, 60 J. INDUS. ECON. 249 (2012) (finding that "enforcement of a FRAND commitment, with damages awarded for excessive license fees, solves the holdup problem, but can retard innovation, and it is even possible that this solution is worse than the problem").

[32] Case C-170/13, *Huawei Technologies Co. v. ZTE Corp.* ¶ 55 (July 16, 2015), http://curia.europa.eu/juris/document/document.jsf?text=&docid=165911&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=603775.

[33] *See* Douglas H. Ginsburg, Taylor M. Owings, & Joshua D. Wright, *Enjoining Injunctions: The Case Against Antitrust Liability for Standard Essential Patent Holders Who Seek Injunctions*, ANTITRUST SOURCE 1, 5-6 (Oct. 2014) (explaining, among other things, that the law of contracts is sufficient to provide optimal deterrence) [hereinafter Ginsburg, Owings, & Wright]; *see also* Bruce H. Kobayashi & Joshua D. Wright, *The Limits of Antitrust and Patent Holdup: A Reply to Cary, et al.,* 78 ANTITRUST L.J. 505 (2012).

[34] *See* Ginsburg, Owings, & Wright, *supra* note 33 at 2-3, 6.

competitive royalties that are not consistent with prior commitments by the SEP holder. This is necessary to avoid the presumption that an SEP holder who seeks injunctive relief will necessarily use that relief (or the threat of it) to demand supra-competitive royalties.[35] That presumption would be unwarranted because market mechanisms impose a number of constraints that militate against acting upon the opportunity for holdup. For example, reputational and business costs may deter repeat players from engaging in holdup and "patent holders that have broad cross-licensing agreements with the SEP-owner may be protected from hold-up."[36] In addition, patent holders often enjoy a first-mover advantage if their technology is adopted as the standard. "As a result, patent holders who manufacture products using the standardized technology 'may find it more profitable to offer attractive licensing terms in order to promote the adoption of the product using the standard, increasing demand for its product rather than extracting high royalties'"[37] per unit.

Furthermore, any liability theory that would require an SEP holder to prove that an accused infringer is an unwilling licensee threatens to deter participation in standard setting, particularly if an accused infringer can prove willingness simply by agreeing to be bound by terms determined in a neutral adjudication. If the worst penalty an SEP infringer faces is not an injunction but merely paying, after adjudication, the FRAND royalty that it should have agreed to pay when first asked, then reverse holdup and holdout give implementers a profitable way to defer payment—or if they are judgment proof, to avoid payment altogether—and puts SEP holders at a disadvantage that reduces the rewards to, and therefore can only discourage, both innovation and participation in standard setting.[38] In short, creating an AML sanction for the mere seeking of injunctive relief is likely to introduce additional delay, or holdout, in FRAND licensing.

Lastly, should the SAIC retain this provision, it should at the very least adopt a safe harbor from AML liability similar to that adopted by the ECJ in *Huawei v. ZTE*.[39] Specifically,

---

[35] *See* Anne Layne-Farrar & Koren W. Wong-Ervin, *Methodologies For Calculating FRAND Damages*, LAW360 at 3-4 (Oct. 8-10, 2014) (explaining that "the actual practice of hold-up requires two elements: opportunity and action," listing a number of market mechanisms that militate against the opportunity for holdup), https://www.ftc.gov/system/files/attachments/key-speeches-presentations/wong-ervin_-_methodologies_for_calculating_frand_damages.pdf.

[36] *See, e.g.*, Prepared Statement of the Federal Trade Commission Before the U.S. Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights Concerning "Standard Essential Patent Disputes and Antitrust Law" at 6 (July 30, 2013), https://www.ftc.gov/sites/default/files/documents/public_statements/prepared-statement-federal-trade-commission-concerning-standard-essential-patent-disputes-and/130730standardessentialpatents.pdf.

[37] *Id.*

[38] Such delay tactics are magnified when the patent owner has a large worldwide portfolio of SEPs requiring it to file lawsuits around the world to adjudicate a FRAND royalty on a patent-by-patent basis. In such cases, international arbitration on a portfolio basis would appear to be the most efficient and realistic means of resolving FRAND disputes.

[39] Case C-170/13, *Huawei Technologies Co. v. ZTE Corp.* (July 16, 2015), http://curia.europa.eu/juris/document/document.jsf?text=&docid=165911&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=603775.

an SEP holder that (1) prior to initiating an infringement action, alerts the alleged infringer of the claimed infringement and specifies the way in which the patent has been infringed; and (2) after the alleged infringer has expressed its willingness to conclude a license agreement on FRAND terms, presents to the alleged infringer a specific, written offer for a license, specifying the royalty and calculation methodology, should be free of liability. The ECJ quite properly put the burden on the alleged infringer to "diligently respond" to the SEP holder's offer, "in accordance with recognized commercial practices in the field and in good faith," by promptly providing a specific written counter-offer that corresponds to FRAND terms, and by providing appropriate security (e.g., a bond or funds in escrow) from the time at which the counter-offer is rejected and prior to using the teachings of the SEP.[40] This approach is necessary to take into account the conduct of both the patentee and the accused infringer when considering whether to impose an AML sanction.

In its decision, the ECJ recognized that SEP holders have "the right to bring an action for prohibitory injunction or for the recall of products," and made clear that the SEP holder's right can be limited only in particular and exceptional circumstances.[41] The decision recognizes concerns about reverse-holdup, stating that the Court will not tolerate infringers' "delaying tactics."[42] The ECJ reiterates, in multiple places throughout the decision, that its competition analysis involves a situation involving two *competitors*, which suggests that the Court's holding and analysis is limited to matters involving competitors. Lastly, the ECJ analyzed the seeking of injunctive relief as possible *exclusionary* conduct as opposed to *exploitative* conduct such as charging excessive or unfairly high royalties.

Chapter VII.31 – Patent Pools

Chapter VII.31 would create a presumption that certain acts taken by a patent pool management organization "without justifiable reason" would "generally have the effect of eliminating or restricting competition." We respectfully urge the elimination of this presumption in favor of an effects-based approach. As the U.S. antitrust agencies and others, including the European Commission and the Competition Bureau of Canada, have recognized, pooling arrangements have the potential to generate significant efficiencies, for example, reducing transaction costs (by allowing "one-stop shopping" for patents needed to implement a standard), reducing patent infringement litigation, clearing blocking positions, and mitigating any potential problems of royalty stacking.[43] As such, the U.S. antitrust agencies analyze pooling arrangements under the rule of reason (an effects-based approach), analyzing the particular pool

[40] *Id.* ¶¶ 66-67.

[41] *Id.* ¶ 65-66, 71.

[42] *Id.* ¶ 55.

[43] DOJ-FTC IP GUIDELINES § 5.5; EUROPEAN COMMISSION, GUIDELINES ON THE APPLICATION OF ARTICLE 101 OF THE TREATY ON THE FUNCTIONING OF THE EUROPEAN UNION TO TECHNOLOGY TRANSFER AGREEMENTS ¶ 176 (2014), http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52014XC0328%2801%29&from=EN; COMPETITION BUREAU OF CANADA, ENFORCEMENT GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY Ex. 8 at 28 (Sept. 18, 2014), http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/cb-eg-ipegs-e.pdf/$file/cb-eg-ipegs-e.pdf.

at issue to determine whether, on balance, the arrangement harms competition.[44] This approach would benefit Chinese consumers because presumptions of competitive harm could have a chilling effect on the creation of procompetitive patent pools by subjecting their organizers to a higher likelihood of liability under the AML.

CONCLUSION

We appreciate the opportunity to comment and would be happy to respond to any questions the SAIC may have regarding this comment.

[44] *See generally* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION 64-66 (2007).