

**Statement of**

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**Before the**

**HOUSE JUDICIARY SUBCOMMITTEE ON COURTS, THE INTERNET, AND  
INTELLECTUAL PROPERTY**

**on the subject of**

**MARKET POWER AND INTELLECTUAL PROPERTY LITIGATION**

**November 8, 2001**

**2:00 p.m.**

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Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to testify on behalf of Intellectual Property Owners Association (IPO). I am the current President of IPO. I am also Chief Intellectual Property Counsel for General Electric Co. in Fairfield, Connecticut, and I have the privilege of serving on the U.S. Patent and Trademark Office's Patent Public Advisory Committee "P-PAC," as First Vice President of the American Intellectual Property Law Association, and on the Council of the IP Law Section of the American Bar Association. The views I am presenting today are those of IPO, and not necessarily those of my company, the P-PAC or any bar association. Speaking for IPO, I am speaking for owners of intellectual property rights.

IPO is an association of U.S.-based owners of patents, trade secrets, trademarks, and copyrights. Our members include about 100 American corporations that are among the largest patent filers in the United States and worldwide from all major industries. Our members file about 30 percent of the patent applications that are filed in the U.S. Patent and Trademark Office (PTO) by U.S. nationals, and pay nearly \$200 million a year in fees to support operations of the PTO.

I am testifying here today largely because, in recent years, IPO has observed the incipient stages of a distressing dilution of intellectual property rights. The Supreme Court long ago recognized that the right to exclude is the "very essence" of the property right a patent confers.

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*Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405, 429 (1908). Yet several courts have recently cast doubt on the continued vitality of this right. Although there previously had been “no reported case in which a court . . . imposed antitrust liability for a unilateral refusal to sell or license a patent or copyright,” *Image Technical Services, Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1217 (9<sup>th</sup> Cir.1997), the Court of Appeals for the Ninth Circuit has broken away from this consistent line of precedent. *See id.* And despite the previously limited application of the “essential facilities” doctrine, courts in this country and abroad have begun to extend the doctrine to intellectual property. *See, e.g., Bell South Adver. & Publishing Corp. v. Donnelley Info. Publ’g*, 719 F. Supp. 1551, 1566 (S.D. Fla. 1988) (concluding that there is “no reason” why the doctrine cannot apply when the alleged essential facility is information), *rev’d on other grounds*, 999 F.2d 1436 (CA11 1993); Joined Cases C-241/91 P & C-242/91 P, *Radio Telefis Eireann v. Commission*, 1995 E.C.R. I-743 (holding by European Court of Justice that information protected by a copyright that was essential to the ability to compete had to be licensed on reasonable terms); Case COMP D3/38.044 – NDC Health/IMS Health (Commission of the European Communities, July 3, 2001) (compelling IMS Health Inc. to grant a copyright license to its “1860 brick structure,” which is a system for organizing pharmaceutical data, on the basis that the structure is an essential facility), *order temporarily suspended, IMS Health Inc. v. Commission of the European Communities*, T-184/01 R (Court of First Instance of the European Communities, Aug 10, 2001).

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This erosion of intellectual property rights has occurred notwithstanding Congressional efforts to protect and strengthen the right to exclude over the past two decades. Since 1984, Congress has amended 35 U.S.C. §271 – the statute that provides the basic definition of patent infringement – seven times. Each amendment made the definition of infringement, and thus the patent holder’s exclusive rights, broader than before. Without exception, these amendments have demonstrated Congress’s commitment to preserving a patentee’s right to exclude. The courts, however, have not heeded Congress’s message and have continued to misunderstand intellectual property rights. In *United States v. Microsoft*, for example, the Court of Appeals for the District of Columbia compared an intellectual property owner’s exercise of the right to exclude with tortious misuse of a baseball bat. *See* 253 F.3d 34 (2001).

In IPO’s view, the judicial presumption that intellectual property establishes market power is simply another manifestation of this erosion of intellectual property rights. As such, it should be eliminated. In lieu of the presumption, courts should analyze allegations of market power the same way in all antitrust cases, whether the property is intellectual or traditional: Courts should simply examine the facts of the particular case. Because antitrust law should not treat intellectual property more harshly than other types of property, IPO supports the proposed legislation.

Congress considered and decided not to enact similar legislation several years ago. We believe, however, that the recent court decisions undercutting intellectual property confirm the need for such legislation today. It is our hope that, in addition to eliminating the improper

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presumption of market power, this legislation will also remind the courts of Congress's consistent and faithful protection of intellectual property rights, and thereby help stem the tide of further erosion.

### **Presuming Market Power is Irrational and Could Deter Innovation, Competition, and Economic Growth**

Commentators have widely agreed that mere possession of a patent or other intellectual property is insufficient to obtain market power. As Professors Areeda and Hovenkamp put it, some intellectual property has no commercial value at all, let alone sufficient value to bestow market power on its owner. *See* Phillip E. Areeda & Herbert Hovenkamp, IIIA Antitrust Law: An Analysis of Antitrust Principles and Their Application 131, ¶523 (1996). A product might possess sufficient inventiveness to be patentable, but there might not be anyone who is willing to pay the cost of production. And even when intellectual property has value, market power is highly unlikely if the relevant market contains numerous competitors or if entry barriers are surmountable. In the markets for toasters, cameras, and home computers, for example, most products contain patented features but still face vigorous competition from viable substitutes. These patented goods are socially useful, and their innovation has augmented consumer welfare, but no producer of the goods can be said to possess market power. To use the blunt words of Professor Hovenkamp, “presum[ing] market power in a product simply because it is protected by intellectual property is nonsense.” Herbert Hovenkamp, *Federal Antitrust Policy: The Law of Competition and Its Practice* 136 (1994).

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Moreover, the federal patent system, and the constitutional grant of authority from which it is derived, are based on the recognition that “[i]nvention is an uncertain business,” and that, “[t]o spur investment in it, inventors must be reasonably assured that they will be able to recoup their costs and earn a profit.” Rochelle C. Dreyfuss, *Dethroning Lear: Licensee Estoppel and the Incentive to Innovate*, 72 Va. L. Rev. 677, 679 (1986). Without the reward of a patent, and the right of exclusive use that it confers, “firms have weak incentives to absorb the costly expenditures needed to develop intellectual property.” Alden F. Abbott, *Developing a Framework for Intellectual Property Protection to Advance Innovation, in Intellectual Property Rights in Science, Technology and Economic Performance* 311, 317 (Francis W. Rushing & Carole G. Brown eds., 1990). They “run the risk that . . . their innovations w[ill] earn insufficient profits to offset the losses stemming from failed research efforts,” and that “capital markets w[ill] be far less willing to provide funds for independent research efforts.” *Id.* at 321.

The patent system fosters innovation and investments in research and development through what the Supreme Court has described as “a carefully crafted bargain.” *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 151 (1989). In exchange for “disclosure and the consequent benefit to the community,” the law gives inventors exclusive rights to practice their inventions for a limited period of time. *Id.* Thus, to foster innovation, the right to exclusive use must effectively compensate inventors, not only for sharing their inventions with the world, but also for investments they make in both successful and unsuccessful research and development

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efforts, and for the risk, particularly acute in the high-tech industry, that their patented innovations may rapidly become obsolete.

The benefit of this bargain, and thus the degree to which it fosters innovation, is significantly reduced or undermined if the reward for innovation and disclosure simultaneously saddles the innovator with a presumption of market power. As then-Deputy Assistant Attorney General Joel Klein explained to this Committee in 1995, “[t]ypically, one of the most important factors in determining whether a civil antitrust law violation has occurred is whether the firm engaging in particular conduct has market power.” Prepared Statement of Joel I. Klein, Deputy Ass’t Attorney General, Antitrust Division, U.S. Department of Justice, in Hearing before the Committee on the Judiciary, House of Representatives, 104<sup>th</sup> Cong., 2<sup>nd</sup> Sess., on H.R. 2674 (May 14, 1996). Thus, a presumption that this important predicate to liability exists greatly increases both the threat of litigation and the risk of a finding of liability. In light of the powerful antitrust litigation tools available in American courts – class action procedures, *parens patriae* actions by the States, reliance on circumstantial evidence – and the powerful remedies available for antitrust violations – treble damages, joint and several liability, and injunctions – a presumption that increases the risk of antitrust litigation and liability attaches a significant disability to the statutory right “to exclude others from making, using, offering for sale, or selling the invention.” 35 U.S.C. §154(a)(1). The inevitable result of altering and reducing the benefit of the patent bargain is to reduce the reward for investment in research and development that is so important to consumer welfare and to the nation’s economy.

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The possibility that a presumption of market power will deter innovation has become even more likely in light of the Ninth Circuit's decision in *Image Technical Services, Inc. v. Eastman Kodak Co.*, 125 F.3d 1195 (1997), which held that, when a seller has market power, his mere refusal to license a patented product to a competitor can violate section 2 of the Sherman Act. The Ninth Circuit based its liability finding on the patent owner's subjective intent – introducing enormous uncertainty into whether an IP owner has the right to refuse to license its intellectual property. Were courts to presume that all patentees have market power, then the effect of *Image Technical Services* would be that all patentees (or at least all patentees in the Ninth Circuit) would have to think twice before refusing to license their patents to competitors, lest the patentees be forced to defend against costly lawsuits under the Sherman Act. The combination of a presumption of market power and the Ninth Circuit's holding limiting the freedom of those who possess market power would open the door to vexatious litigation against those who own intellectual property. This result would obtain, notwithstanding the fact that the very essence of a patent has always been “the right to exclude others from making, using, offering for sale, or selling the invention,” 35 U.S.C. §154(a)(1). Fortunately, the Court of Appeals for the Federal Circuit rejected the Ninth Circuit's analysis and holding. *In re Independent Service Organizations Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000). But patent holders who may face litigation in the Ninth Circuit will have to be cautious before exercising their fundamental patent rights, especially if courts are permitted to apply the economically baseless presumption that all intellectual property establishes market power.

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### **Legislation is Necessary to Clarify that Courts Should Not Presume Market Power**

Legislation would not be needed if federal courts had soundly settled the expectations of intellectual property owners by uniformly rejecting the presumption of market power.

Unfortunately, however, in older decisions, the Supreme Court has twice suggested that the presumption should exist, the courts of appeals are divided in their holdings, and the Supreme Court has chosen not to revisit the issue in nearly twenty years. Almost 40 years ago, in an overbroad statement unnecessary to the holding of the case at hand, the Supreme Court stated that the “economic power” required for a tying violation is “presumed when the tying product is patented and copyrighted.” *United States v. Loew’s, Inc.*, 371 U.S. 38, 44 (1962). Citing to this language, the Supreme Court reiterated its position over two decades later, suggesting in *dictum* in another tying case that, “if the government has granted the seller a patent or similar monopoly over a product, it is fair to presume that the inability to buy the product elsewhere gives the seller market power.” *Jefferson Parish Hosp. Dist. v. Hyde*, 466 U.S. 2, 16. In a well-reasoned concurring opinion, Justice O’Connor flatly rejected this presumption and explained (as IPO has done today) that a patent holder lacks market power when there are close substitutes to the patented products. *Id.*, at 38 n.7 (1984). But her position garnered only four votes, and the lower courts were left to choose between the misguided dictum of the majority and the concurring opinion of Justice O’Connor.

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Taking the latter course, most courts of appeals have recognized that a presumption of market power is economically baseless. *See, e.g., A.I. Root Company v. Computer/Dynamics, Inc.*, 806 F.2d 673 (6<sup>th</sup> Cir. 1986); *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665 (7<sup>th</sup> Cir. 1985). The Court of Appeals for the Ninth Circuit, however, has maintained that the presumption applies with respect to patents and copyrights in tying cases. *Digidyne v. Data General Corp.*, 734 F.2d 1336 (9<sup>th</sup> Cir. 1984). Because the decisions of the Ninth Circuit affect the legal rights of over 50 million people living in nine western states – an area that includes much of our nation’s high-tech industries – as well as the rights of any national or global company doing business in this large and populous area, that court’s presumption of market power has tremendous consequences. Many onlookers have hoped that the Ninth Circuit would overturn its decision or that the Supreme Court would resolve the issue,<sup>1</sup> but neither event has occurred. Indeed, on several occasions in recent years, the Supreme Court has opted not to hear a case that squarely presented the question. *See, e.g., id.*, cert. denied, 473 U.S. 908 (1985); *American Hoist & Derrick Co. v. Sowa & Sons, Inc.*, 725 F.2d 1350 (Fed. Cir.), cert. denied, 469 U.S. 821 (1984); *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665 (7<sup>th</sup> Cir. 1985), cert. denied, 475 U.S. 1129 (1986). Thus, the federal courts have not settled the issue, and intellectual property owners have been confronted with uncertainty, insecurity and the risk that their actions will result in significant litigation costs and possibly even treble damages.

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<sup>1</sup> *See, e.g.*, Prepared Statement of Joel I. Klein, Deputy Ass’t Attorney General, Antitrust Division, U.S. Department of Justice, in Hearing before the Committee on the Judiciary, House of Representatives, 104<sup>th</sup> Cong., 2<sup>nd</sup> Sess., on H.R. 2674 (May 14, 1996).

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The Department of Justice and the Federal Trade Commission, to be sure, have published Antitrust Guidelines for the Licensing of Intellectual Property, stating that the agencies “will not presume that a patent, copyright, or trade secret confers market power upon its owners.” *Antitrust Guidelines for the Licensing of Intellectual Property* (1995). These guidelines, however, are just that – guidelines. They do not bind any court; nor do they preclude private parties from filing law suits for treble damages. Indeed, the guidelines are not even permanent, as any administration can change them at any time. Consequently, despite the agencies’ welcome efforts, the existing confusion among the federal courts may deter parties from entering into beneficial marketing or licensing arrangements. For meaningful security against vexatious lawsuits and flawed judgments in antitrust cases, intellectual property owners and developers need legislation abolishing the presumption of market power.

### **Without the Presumption, Courts Can Simply Apply the Factual Analysis That They Use in Other Antitrust Cases**

Eliminating the presumption of market power will not create an antitrust exemption; it will not legalize any conduct that is currently illegal. Eliminating the presumption simply requires a plaintiff suing a patent holder – like plaintiffs suing the owners of other property – to prove that market power does, in fact, exist. Courts, in turn, would resolve that issue employing the same factual analysis that they use in other antitrust cases. Courts would examine, among other factors, the availability and closeness of substitutes, the existence of entry barriers, the defendant’s market share, and the number and size of other sellers and buyers. Courts have

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experience applying this fact-based analysis. Not only is it generally used with respect to traditional property, but most courts have employed it in the context of intellectual property. Indeed, the Supreme Court has suggested that a factual analysis of the “relevant market” is required when the antitrust claim is one of monopolization or attempted monopolization under section 2 of the Sherman Act, even if the case involves intellectual property. *Walker Process Equipment, Inc. v. Food Machinery and Chemical Corp.*, 382 U.S. 172 (1965); *see also Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447 (1993). Because courts have routinely applied the fact-based analysis of market power, and have done so for several decades without substantial conflict in results, IPO has confidence that courts can faithfully and consistently apply the analysis without any difficulty.

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We recognize that the Sherman Act, like the patent statute, plays an important role in fostering innovation and consumer welfare, and that some members of this Committee have in the past expressed concerns about amending in any way a law that has served as the charter of economic liberty. A presumption that a patent confers market power, however, is inconsistent with the common aims of both statutes. Recognizing the import of intellectual property to our nation’s vitality, the Framers of our Constitution expressly empowered Congress “[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors

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the exclusive Right to their respective writings and Discoveries,” U.S. Const., Art I, §8, ¶8.

Intellectual property plays no less a role in preserving the general welfare today than it did some 200 years ago. As evidenced by the economic explosion of the 1990s, intellectual property can pave the way for overwhelming gains in productivity and consumer welfare. The fact that economic prospects may have dimmed in recent months only lends support to the argument for protecting intellectual property and encouraging entrepreneurs to create and develop competitive new products. Because the proposed bill provides such protection and encouragement, IPO supports it.

IPO again thanks the Chairman and the Subcommittee for the opportunity to testify in favor of the proposed legislation.