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DEPARTMENT OF JUSTICE ANTITRUST DIVISION

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and FEDERAL TRADE COMMISSION

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Hearing on:

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COMPETITION AND INTELLECTUAL PROPERTY LAW

10

AND POLICY IN THE KNOWLEDGE BASED ECONOMY

11

Strategic Use of Licensing: Is There Cause

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For Concern about Unilateral Refusals to Deal?

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Wednesday, May 1, 2002

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Great Hall of the U.S. Department of Justice

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333 Pennsylvania Avenue, N.W.

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Washington, D.C.

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1 PARTICIPATING PANELISTS:

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3 Ashish Arora, Associate Professor Economics,

4 Carnegie Mellon University

5 Jonathan Gleklen, Arnold & Porter

6 Paul Kirsch, Townsend and Townsend and Crew

7 Benjamin Klein, Professor of Economics,

8 University of California, Los Angeles

9 Jeff MacKie-Mason, Arthur W. Burks Professor of

10 Information and Computer Science and

11 Professor Economics and Public Policy,

12 University of Michigan

13 A. Douglas Melamed, Wilmer, Cutler & Pickering

14 Carl Shapiro, Transamerica Professor of Business

15 Strategy and Professor of Economics,

16 Haas School of Business, and Director,

17 Institute of Business and Economic

18 Research, University of California,

19 Berkeley

20 Chris Sprigman, King & Spaulding

21 Mark Whitener, Antitrust and General Counsel,

22 General Electric

1 MORNING SESSION

2 (9:30 a.m.)

3 HEWITT PATE: Good morning. I'm
4 Hewitt Pate, one of the deputies at the Antitrust
5 Division. I'd like to welcome everyone today to
6 our hearing. Thank you all for coming.

7 It looks like we've got a good group
8 here to hear what I think is going to be a
9 terrific panel on refusals to license. The title
10 of the program is Strategic Uses of Licensing:
11 Is There Cause for Concern About Refusals to
12 License?

13 Before I introduce the program
14 somewhat, I want to especially thank Frances
15 Marshall and Susan DeSanti from the FTC for all
16 their work in putting these hearings together,
17 and personally thank Pam Cole, Sue Majewski,
18 and Howard Blumenthal for helping with the
19 preparations today.

20 We're here to talk about as it's
21 most usually described whether there is a tension
22 between antitrust and intellectual property, a

1 different view of whether antitrust liability
2 might lie for a refusal to license, at least an
3 unconditional refusal to license in the CSU case,
4 and went on to say in some dictum that has been
5 the subject of much discussion that antitrust
6 liability for a refusal to license could not
7 exist except in the context of tying, fraud on
8 the Patent Office, or sham litigation.

9 We're going to talk today primarily
10 about unconditional refusals to deal. Other
11 sessions have dealt with licensing terms and
12 conditioning that are of interest in these
13 hearings.

14 I think as one of the papers for this
15 panel said, my own concern in listening to this
16 is not whether there is some abstract concern
17 about licensing practices, but whether there are
18 really situations in which it would be
19 appropriate for Courts to impose antitrust
20 liability.

21 I have some views on that. But from
22 the Division and the FTC's perspective, we're

1 here today to listen to a terrific panel.
2 Among the questions I think that will be very
3 interesting to have discussed is this underlying
4 question of whether there is a difference between
5 IP and other forms of property for purposes of
6 applying the antitrust laws.

7 Certainly as it's described in
8 litigation you often see arguments made that of
9 course IP is different because it's mentioned in
10 the Constitution, whatever that would mean, or
11 because it is a right to exclude as though that
12 necessarily implies that IP is different from
13 other forms of property.

14 There are other ways in which it
15 might be though. Certainly the statutory scope
16 of a patent right deserves examination. And if
17 Congress defines the scope of a patent right in
18 a way that differentiates it from other property,
19 that's something that obviously deserves
20 consideration.

21 Secondly, I think we have some well
22 qualified panelists who will discuss whether

1 there is an economic difference between the
2 two forms of property, whether the ease of
3 reproduction of intellectual property, at
4 least intellectual property of some forms,
5 is a differentiating factor.

6 Another question is whether there
7 are situations or what situations there are where
8 the owner of any type of property whether IP or
9 otherwise really does have a duty to refrain
10 from unconditional refusals to deal.

11 Aspen Skiing is a case that's much
12 discussed. But of course there was a prior
13 course of conduct. And I think it will be
14 interesting to hear from the panel as to what
15 situations there are where a blanket and
16 unconditional refusal to deal should raise
17 antitrust concerns.

18 What about other forms of intellectual
19 property, trade secrets and copyrights, for
20 example? I'll put aside trademark which I think
21 of as a type of IP that's really for a different
22 purpose than the ones we're concerned with.

1 The two main cases deal with patents,
2 and those seem to be the predominant form of IP
3 that's discussed. But is there a reason that
4 trade secrets or copyrights should be subject to
5 a different form of analysis?

6 I think it would seem odd to
7 most people to imagine a Court requiring the
8 disclosure of trade secrets. Is that because
9 there really is a difference between trade
10 secrets and patents as it relates to antitrust
11 law?

12 Or if it is odd to think of a Court
13 compelling that, does that call into question the
14 extent to which a required license is needed in
15 the patent context?

16 And how are Courts to administer
17 disclosure of trade secrets, for example, if
18 that -- if the principles of a required duty to
19 deal obtain there? Even in the patent context
20 sometimes the use of a patent requires underlying
21 know-how and trade secrets, trade secret
22 disclosure perhaps.

1 Would under the Kodak analysis, for
2 example, there ever be a claim that the service
3 personnel of an ISO have an antitrust entitlement
4 to training from the equipment manufacturer?

5 And finally I'll end with this. I
6 wonder how big a problem or how fundamental a
7 problem is this? The question gets posed as one
8 of a fundamental tension between antitrust and
9 IP.

10 Is it that, or are these cases really
11 just an outgrowth of the Supreme Court's Kodak
12 decision and the Supreme Court giving a green
13 light potentially to the establishment of
14 antitrust liability in a situation where that
15 hadn't been thought very likely before?

16 Maybe another way to ask that is
17 whether the Division was right in 1991. So with
18 that let me turn the program over to Pam Cole who
19 will handle some housekeeping issues and then
20 introduce our panelists.

21 PAM COLE: Good morning. Yes. I get
22 to handle some housekeeping issues. I hire

1 somebody at home to do that, but I'm going to do
2 it here. Let me just talk a little bit about
3 just some basic nuts and bolts issues.

4 We're in the Great Hall of the Justice
5 Department, as I'm sure you are all aware, which
6 means that in order to leave this room you need
7 to be escorted. We do have paralegals in the
8 back of the room wearing green name tags, and
9 they will escort you wherever you need to go.

10 If you need to make a phone call, you
11 should go up to the seventh floor. I guess cell
12 phones don't work here. And they will escort you
13 up to the seventh floor.

14 The timing of this is such that we
15 are going to end the morning session at noon,
16 have about an hour and a half break for lunch,
17 reconvene at 1:30, and then end the session at
18 4:00.

19 For the sake of the panelists in terms
20 of the microphone, if you can talk right into the
21 microphone -- and it may not come on until a few
22 seconds after you pull it close to you. So it

1 will be working. You just need to wait a little
2 bit of time.

3 Let me just make some introductions
4 of the panelists. My name is Pam Cole. I'm an
5 attorney with our San Francisco office of the
6 Justice Department, and it's great to be here in
7 Washington, D.C. I've been here since last week
8 at the spring meeting, so I'm eager to get home.
'pcerltw my right. MEd PolkngtHent, attooffice o'm an

1 cannot do their biographies justice in terms of
2 the extensiveness of their qualifications. But
3 for the sake of time I'm just going to make some
4 short introductions.

5 I also want to say personally that
6 after are viewing all of the panelists'
7 presentations I really appreciate the amount of
8 work and thought that all of you have put into
9 these presentations. And I sincerely mean that.

10 I never thought that refusals to
11 license could be as interesting as all of you
12 have made it in your presentations. And I think
13 this is really going to be a fun panel.

14 So Jonathan Gleklen is a
15 partner at Arnold & Porter in Washington, D.C.
16 Jonathan served as counsel to Xerox in the In
17 Re: Independent Service Organizations antitrust
18 litigation case. That's more commonly known as
19 the CSU case. And obviously that case is going
20 to be subject to extensive discussion in today's
21 session.

22 Next up will be Chris Sprigman. Chris

1 served as -- Chris is currently counsel at King &
2 Spaulding in Washington, D.C. Prior to joining
3 the firm Chris served as appellate counsel to the
4 Antitrust Division of the Department of Justice.
5 In both capacities Chris has focused on the

1 intellectual property rights, and technology
2 licensing.

3 Following Ashish will be Paul Kirsch.
4 Paul Kirsch is a neighbor of mine and also a
5 partner at Townsend and Townsend and Crew in
6 San Francisco. Paul's practice includes both
7 intellectual property and antitrust. And he
8 extensively represents the antitrust plaintiffs.
9 Paul is one of the attorneys who represented
10 Intergraph in the Intergraph versus Intel
11 antitrust and intellectual property litigation.

12 Carl Shapiro will be next. Carl, for
13 those of you who don't know him, which I'm sure
14 many of you do, is the Transamerica Professor of
15 Business Strategy at the Haas School of Business
16 at the University of California at Berkeley.

17 He is also is director of the
18 Institute of Business and Economic Research
19 and professor of economics in the economics
20 department at UC-Berkeley. Professor Shapiro
21 also served as deputy assistant attorney general
22 for economics in the Antitrust Division of the

1 U.S. Department of Justice during 1995 to 1996.

2 Following Carl will be Jeffrey

3 MacKie-Mason. Jeffrey is the Arthur W. Burks

1 mostly guide the discussion.

2 And what I'd like the panelists to do
3 is after a particular presentation if you have
4 a comment or question about the presentation, if
5 you could just turn your name tags on their side
6 like this. And we will call on you for your
7 questions or comments which will hopefully
8 facilitate discussion.

9 And I think that is about it. So why
10 don't we start with Jonathan. And, panelists,
11 you're free to go up to the -- if you're doing
12 a PowerPoint especially, you should go up to the
13 podium or whatever you want to do.

14 JONATHAN GLEKLEN: I'd like to thank
15 the Department of Justice and the FTC for having
16 these hearings. It's an important topic, and
17 it's one that I've basically built my entire
18 career on. I'm Jon Gleklen. I'm a partner
19 at Arnold & Porter.

20 And I've been working on the Xerox ISO
21 litigation since the summer of 1992 when I was a
22 summer associate. So the first disclaimer is

1 I don't stand here representing anybody's views
2 other than my own, not Arnold & Porter's, not its
3 clients, not even Xerox's.

4 Pam asked me to start out by talking
5 a little bit about the Xerox case and the facts
6 and the decision and what to make of it, just
7 to clarify what the case is and isn't about,
8 something that I admit is hard to do by reading
9 the Federal Circuit's decision.

10 I've done this in more detail in an
11 article that's available in the back, and it will
12 be up on the website. But the short facts are
13 Xerox makes, sells, services copiers and
14 printers.

15 And CSU, Copier Services Unlimited,
16 was an ISO, an independent service organization
17 that serviced those copiers and printers.
18 Starting in 1984 Xerox unilaterally decided that
19 it was no longer going to sell parts to ISOs.

20 It later decided not to sell software
21 as software became more a component of the
22 copiers and printers it was selling. Xerox

1 didn't agree with anybody. It was a completely
2 unilateral decision. Xerox unlike Kodak didn't
3 agree with its customers that the customers would
4 not supply parts or software to ISOs.

5 Customers were free to and in fact
6 did buy parts from Xerox and sell them to ISOs.
7 Xerox simply unilaterally decided we're not going
8 to sell parts to ISOs except to the extent that
9 they are also end users. There was a class
10 action litigation. Xerox settled it in 1994 by
11 agreeing to sell parts to ISOs, directly to ISOs.

12 And everybody ended up getting the
13 same prices and the same quantity discounts, with
14 a single exception which was the U.S. Navy which
15 had a cooperative service agreement with Xerox
16 where Xerox serviced the copiers while they were
17 in port and the Navy serviced them when they were
18 out at sea.

19 CSU opted out of the settlement of the
20 class action and filed their own lawsuit. CSU
21 challenged a couple of things. They challenged
22 Xerox's past, pre-'94 refusal to sell parts and

1 license software and Xerox's current '94 and
2 thereafter pricing, saying that those were also
3 exclusionary.

4 And CSU's theory was basically the
5 Kodak theory. Xerox has a parts and software
6 monopoly, and it is leveraging that monopoly to
7 obtain or maintain a monopoly in a market for
8 the service of Xerox's copiers and printers.

9 Like I said, their only conduct at
10 issue was unilateral. The only claims were
11 section II claims, no section 1 claims, no
12 tying, no concerted refusal to deal. Xerox
13 counterclaimed patent/copyright infringement plus
14 some trademark and state law claims.

15 And Xerox's argument was that CSU
16 had used infringing parts, these third-party
17 parts vendors had sprung up, they made parts that
18 infringed Xerox's patents, CSU bought and used
19 those;

20 And that CSU had essentially stolen
21 disks containing diagnostic software and upgraded
22 diagnostic software, had reproduced that software

1 by installing it on copiers and printers, and
2 then infringed the copyrights again by using the
3 software which was unlicensed.

4 The nice thing about the Xerox case
5 is that it's a pure law school case. There are
6 essentially no disputed issues of fact at the
7 end of the day. CSU conceded that all of their
8 injury was attributable to Xerox's refusal to
9 sell or license patented and copyrighted
10 materials.

11 Basically they said there's no
12 but-for causation; if we can't get the patented
13 photoreceptors and the patented and copyrighted
14 diagnostic software, we're out of business; so
15 the only thing that matters is the patented
16 stuff. CSU conceded the infringement of the
17 patents and copyrights.

18 And their only defense was a misuse
19 defense. So the remaining issues, as I said,
20 were pure questions of law. And there are
21 basically three of them:

22 Can a pure unilateral refusal to sell

1 and license software or parts covered by patents
2 and copyrights violate section II?

3 Can, quote, unquote, high prices,
4 whatever that means, violate section II because
5 it's anticompetitive conduct? And can this past
6 refusal to sell or the ongoing high prices be
7 misuse?

8 The District Court -- if you go on
9 Westlaw, you'll see that there are literally a
10 half dozen District Court decisions on summary
11 judgment and various motions for reconsideration.
12 But after you parse the various District Court
13 decisions, you basically get to four key
14 holdings.

15 One is that unilateral refusals to
16 deal are neither anticompetitive under section II
17 nor inequitable conduct or whatever the
18 standard would be for misuse. High prices for
19 intellectual property are neither anticompetitive
20 nor misuse.

21 The number of markets, antitrust
22 relevant markets affected by a refusal to license

1 exceptions to the right to unilaterally refuse
2 to license which don't make any sense so -- as
3 Hugh Pate said, tying, fraud on the PTO, and sham
4 litigation. Well, tying is not a unilateral
5 refusal to deal. So tying is not an exception
6 to your right unilaterally to refuse to deal.

7 Fraud on the PTO, well, that doesn't
8 make any sense because if you committed fraud on
9 the PTO you don't have valid IP. So there is no
10 valid IP that you have refused to license. And
11 then the last exception is also wrong I think,
12 sham litigation. This just doesn't make any
13 sense to me.

14 You could engage in sham litigation,
15 and the sham litigation itself might be unlawful,
16 but that doesn't -- it's not clear to my why the
17 underlying refusal to deal should be unlawful.
18 Think of the hypo of a plaintiff -- I'm sorry.

19 An IP owner wants to make sure
20 they get Federal Circuit jurisdiction because,
21 God knows, they don't want to be in the Ninth
22 Circuit. So they say we're going to file

1 addressing Chairman Pitofsky's or former Chairman
2 Pitofsky's concerns that he expressed in I guess
3 two speeches and in an article. One concern is,
4 you know, the Xerox decision could -- or people
5 call it the CSU decision. I call it the Xerox
6 decision.

6 decisio2eechetou the itairPr9.7lfix Tf, inconcam Tj guess

1 Pitofsky gave is, you know, there's essentially
2 a price fixing or a vertical price fixing
3 conspiracy with a licensor and its licensees.

4 And you terminate somebody who breaks
5 with the price fixing conspiracy. The underlying
6 price fixing conspiracy is unlawful.

7 The termination may -- it seems to me
8 irrelevant whether the termination of the guy
9 because he breached -- he didn't go along with
10 the price fixing conspiracy, whether that's
11 lawful or not doesn't make a difference.

12 And fraud on a standard setting
13 organization just seems to me like the sham
14 litigation. It's the underlying fraud that's
15 the anticompetitive conduct. The subsequent
16 unilateral refusal to deal, whether or not that's
17 unlawful really doesn't make a difference.

18 Let me talk briefly about why I think
19 the Federal Circuit got it right in Xerox though,
20 as I say, you wouldn't know why from reading the
21 opinion. I think it is compelled by Supreme
22 Court precedent. And it is in fact consistent

1 with every lower Court's decision except for the
2 Ninth Circuit's.

3 I think the result is compelled by the
4 language in the legislative history of the patent
5 act. And finally I don't think there are any
6 good alternatives to the rule that the Federal
7 Circuit came up with.

8 The Supreme Court has been consistent
9 that a patent or copyright conveys a right to
10 refuse to deal. Leave aside the issue of whether
11 that can be antitrust -- cause antitrust
12 liability.

13 I've put the cases up on the
14 PowerPoint from cases from Continental Paper Bag
15 that exclusion of competitors is the very essence
16 of the right conferred by the patent, to Dawson,
17 to Stewart which is a copyright case.

18 You know, the copyright owner has the
19 capacity arbitrarily to refuse to license one who
20 seeks to exploit the work. So I think we have
21 common agreement that the IP laws themselves
22 convey this right. So the question is: What

1 do the antitrust laws say about that?

2 And I think the Supreme Court
3 precedent though not specifically addressing
4 the unilateral refusal to deal point is pretty
5 consistent that if conduct is authorized by the
6 IP laws it doesn't violate the antitrust laws.

7 So there's the famous Simpson dicta,
8 the patent laws in pari materia with the
9 antitrust laws and modify them pro tanto.

10 To translate that into English, the
11 patent laws and the IP law -- and the antitrust
12 laws address the same subject. And the patent
13 laws modify the antitrust laws as far as they,
14 that is the patent laws, go. And I think the
15 Supreme Court was clearly saying patents are
16 different.

17 In Simpson they were distinguishing
18 U.S. versus General Electric. They said there
19 we said -- you know, everybody may agree the
20 decision is wrong now. But they say in U.S.
21 versus General Electric we said resale price
22 maintenance is lawful. But that was a patent

1 case. And patents are different.

2 So I think Simpson clearly stands for
3 the proposition that the Supreme Court recognizes
4 that there are differences where the IP laws give
5 you rights.

6 Precision Instrument Manufacturing,
7 United Shoe, you know, a patentee's exercise
8 of its right to exclude others from use of the
9 invention is not an offense against the antitrust
10 act. Admittedly none of these cases were
11 directly addressing a unilateral refusal to
12 deal.

13 But there are lower court cases that
14 do. And those are with the exception of the
15 Ninth Circuit pretty consistent. SCM versus
16 Xerox, this is really the same thing as an ISO
17 case now.

18 Xerox had patents on parts that it was
19 refusing to license to an equipment competitor,
20 not a service competitor. SCM was an equipment
21 competitor, exactly the same issue.

22 The Court says Xerox's refusal to

1 license the xerography patents was permissible
2 under the patent laws and therefore does not
3 give rise to antitrust liability. You've got the
4 Miller case. If you lawfully acquire your IP you
5 don't violate section II by maintaining that
6 monopoly by refusing to license.

7 And there are other ISO cases: Data
8 General in the First Circuit, Service & Training
9 in the Fourth Circuit. Like I said, I think it's
10 not just the case law. It really is the patent
11 act. 217(d)(4) in the 1988 amendments to the
12 patent act I think is the most directly on point:

13 No patent owner otherwise entitled
14 to relief for infringement or contributory
15 infringement shall be denied relief or deemed
16 guilty of misuse or illegal extension of the
17 patent by reason of having done one or more of
18 the following, and then listing refuse to license
19 or use any rights to the patent.

20 Now, all of that language other than
21 refuse to license or use any rights to the patent
22 was there in 1951. So the relevant legislative

1 history is the 1951 legislative history. And the
2 Antitrust Division opposed that original 1951 law
3 saying it would carve out an area in which the
4 antitrust law does not operate.

5 And then it's not on the PowerPoint,
6 but if you look at the legislative history Wilbur
7 Fugate who testified for the Antitrust Division
8 said, quote: The proponents of the bill indicate
9 that such a result is contemplated in the
10 language of 217(d). So that's the legislative
11 history of the original act.

12 You've got the 1980 amendment which is
13 just add one more type of conduct onto the long
14 list that already existed of things that were not
15 misuse. The sponsor, Representative Kastenmeyer,
16 says what we're doing is we've got SCM; that's
17 good law; basically we want to codify that law.
18 Look at the language.

19 The language is repetitive if
20 antitrust claims are covered. Misuse or illegal
21 extension, unless that means misuse or -- misuse
22 which is not usually the way we interpret

1 statutes, the legal extension has to mean
2 something else.

3 And finally, you know, barring misuse
4 is pointless if the same conduct violates the
5 antitrust laws.

6 If Congress intended to say you can
7 do this and still have your patent enforceable,
8 if the same conduct violates the antitrust laws,
9 plaintiff is entitled to an injunction saying you
10 can't do this anymore. So it would be pointless.

11 Let me then turn to basically what's
12 the alternative. Well, you have the leveraging
13 theory which comes out of footnote 29 in Kodak.
14 What are the problems with this? First of all,
15 it is not clear to me that anybody who espouses
16 this has really been serious about this one
17 market, two market thing.

18 Even CSU basically said, you know,
19 you can refuse to license Kodak in the equipment
20 market, but you can't refuse to license us. And
21 I don't think there's any principle there other
22 than there is a special rule for ISOs, and the

1 The Court says we are addressing
2 tying. And it was in a case that doesn't involve
3 intellectual property although IP was later an
4 issue in the Kodak case. The record before the
5 Supreme Court is crystal clear. It's in the
6 brief that Kodak did not raise its IP rights.

7 And the plaintiffs actually said, you
8 know, we asked Kodak do you have any IP rights,
9 and they said no. Another alternative: Well,
10 let's just treat patents like any other kind of
11 property, no special rule for IP. So we can
12 apply the same rules that we use for regular
13 property.

14 So there's the intent test from
15 Colgate and Lorain Journal. And pretext is like
16 the intent test, and that's the Ninth Circuit's
17 test. The intent test comes from the famous line
18 from Colgate which starts out: In the absence of
19 any purpose or effect to create a monopoly, you
20 have a right to refuse to deal.

21 The problem here is that intent is
22 meaningless. The purpose of IP is to exclude.

1 It kind of doesn't make any sense to say you
2 refuse to license your IP with the intent to
3 exclude people because that's the right that
4 Congress gave you. Look at professional real
5 estate investors.

6 This is what the precedent says. To
7 condition a copyright upon a demonstrated lack
8 of anticompetitive intent would upset the notion

1 horror.

2 Why anybody would want to extend the
3 essential facilities doctrine beyond the very
4 narrow range of cases hopefully in the distant
5 past to which it's going to apply is beyond me.
6 I recognize that the precedent is ambiguous,
7 reject it as a matter of law in SCM where the
8 plaintiff cited Otter Tail.

9 Some District Courts have rejected
10 it. Other Courts seem to have assumed that the
11 essential facilities doctrine could apply but
12 just chose not to apply it. It's got the same
13 practical problems as the intent test.

14 You have the Federal Circuit's rare
15 cases, quote, unquote, where you won't frustrate
16 the objectives of the copyright act. They give
17 the example of unlawfully acquired IP. I don't
18 know why you should have antitrust liability for
19 refusal to deal there as opposed to antitrust
20 liability for the unlawful acquisition.

21 And it's hard to think of any
22 other examples other than unlawful acquisition.

1 Remember, if unlawful refusals -- if refusals to
2 deal are unlawful, so are high prices. I put up
3 this nice quote from CSU's chairman because it is
4 so entertaining:

5 We're prepared to give Xerox 200 to
6 300 percent mark-up. We would ask the Court to
7 say that a 200 percent to 300 percent mark-up
8 over an objective standard with respect to cost
9 is a sufficient margin for anybody, including
10 ladies' dresses.

11 I don't think we want the Courts
12 treating IP the same as ladies' dresses. How do
13 you figure out what's an unlawfully high price?
14 It's perfectly rational for the IP owner to
15 charge his indifferent price; I would have made
16 this much profit if I had refused to license.

17 It's theoretically rational for the
18 licensee or the putative licensee to pay
19 anything -- any fee up to 100 percent of its
20 economic profits. How do you show that that's
21 exclusionary or bad intent? I don't think
22 there's a workable way of doing it.

1 And again if high prices are lawful,
2 what benefit do we really get from barring
3 refusals to license? If you can choose any price
4 and we're not going to have the Courts inquire
5 into the price, how is the world a better place,
6 bottom line?

7 The decision theoretic approach,
8 it's in a recent Antitrust Law Journal article
9 that analyzed tying. Basically how many false
10 positives, how many false negatives? This
11 to me suggests a rule of per se legality.

12 If we agree that there are at most
13 very limited and at the at least no circumstances
14 under which a unilateral refusal to license
15 should violate the antitrust laws -- and there
16 are real costs to false positives in terms of
17 lost incentive to license.

18 And there are even costs for true
19 negatives of defending the case. There are real
20 costs here. And I don't see any significant
21 benefits, modest benefits at best unless we're
22 going to have the Courts governing what you

1 can charge for IP.

2 I close by saying, look, the antitrust
3 laws are a blunt instrument; you have treble
4 damages; you've got the cost of litigation. I
5 recognize that there are areas where we may all
6 agree that refusals to license are a real
7 problem.

8 What I'd suggest is the remedy is
9 not treble damages and attorneys' fees and
10 turning the plaintiffs' bar loose. But if it's a
11 problem, have Congress enact statutory compulsory
12 licensing as they have done in certain
13 circumstances under the copyright act.

14 Then you don't face treble damages.
15 Everybody knows what the rules are. Everybody
16 can follow the rules. Thanks.

17 (Applause.)

18 CHRIS SPRIGMAN: Hi. Jon Gleklen and
19 I begin in agreement which is that the only clear
20 part of the Fed. Circuit's decision in Xerox was
21 that the Fed. Circuit affirmed a District Court
22 holding that allowed a unilateral refusal to deal

1 and basically declared it immune from antitrust
2 liability.

3 What interests a lot of antitrust
4 lawyers and what alarms some of them is not that
5 bit of clarity. It's the relative sea of murk.
6 And I wanted to spend a little bit of time
7 exploring some of the murk.

8 First of all, the question arises
9 whether the Xerox holding is limited to
10 unilateral refusals to deal or whether it applies
11 more broadly to other kinds of refusals to deal,
12 refusals that are the result of agreement.

13 And the reason this concern arises in
14 large part is because one of the exceptions to
15 the holding that the Federal Circuit noted was
16 tying. Tying agreements come outside of the
17 Xerox rule of per se legality. Well, tying isn't
18 usually unilateral or usually thought of as
19 unilateral.

20 And so that raises the question, well,
21 if they noted one condition that comes outside of
22 the rule, what about all the other kinds of

1 conditions that appear in licenses, the kinds of
2 conditions that we see analyzed in the agency's
3 IP guidelines, for example, exclusive dealing
4 provisions that tie out competing products from
5 distribution;

6 Or non-compensatory discount
7 structures of the type that Professor Ordover
8 analyzed in an article that have no compensatory
9 points along their curve and therefore are seen
10 as non-profit maximizing at any point and a
11 simple foreclosure device;

12 Or grantbacks, especially broad and
13 exclusive grantbacks that have potential effects
14 on innovation incentives and create antitrust
15 concern for that reason.

16 Now, these are provisions in licenses
17 that you see from time to time. They are
18 generally subject to rule of reason analysis.
19 Are these provisions left out of the exceptions
20 to the Xerox rule? Probably not. I don't think
21 that's the right reading of Xerox.

22 The Solicitor General filed a brief

1 when the Supreme Court asked for his views saying
2 that they don't think that's the right reading of
3 the case. But it's not so clear that it isn't.

4 And there's a District Court of
5 Northern California in March of 2000, an
6 opinion in the case Townsend versus Rockwell
7 International that basically used a lesser
8 included rights rationale to say in effect that
9 if in fact you as a patent holder have the right
10 to refuse to license, you have the right to
11 pretty much do anything else short of that.

12 You have the right to put conditions
13 into licenses without fear of liability. The
14 District Court didn't mention the right to fix
15 prices, but one would question whether in fact
16 that is a lesser included right within the right
17 to refuse to license. I don't know if the
18 District Court would go even that far.

1 had been an agreement to license only on the
2 basis of licenses that included conditions of
3 cross-licensing and other forms of reciprocal
4 dealing.

5 The Court essentially ignored the fact
6 that there was the allegation of an agreement and
7 said, well, the licensor can do what it wants as
8 a lesser included right. I'm not so sure that
9 Townsend can be blamed on Xerox. But there it

1 that unilateral refusals to deal is the territory
2 of the Xerox case.

3 Is that narrower rule of more or less
4 per se legality for a refusal to license right?
5 Well, Jon Gleklen said and others have said that
6 it kind of has to be definitionally because the
7 patent is a right to exclude, and a refusal to
8 license is merely an exercise of the right to
9 exclude.

10 That makes sense in a kind of
11 tautological way. But think for a moment about
12 what the right to exclude actually is. If you
13 look at other forms of property, the right to
14 exclude is an essential part of what we think of
15 as property generally, your house, your store,
16 your factory.

17 Much of your ability to enjoy and to
18 make money from that asset stems from your right
19 to exclude.

20 And generally although refusal to deal
21 laws are in the area of some doctrinal confusion
22 and concern, especially with respect to the

1 essential facilities leg of it, we generally
2 think that your right to refuse to deal in
3 tangible forms of property runs out where your
4 refusal to deal liability begins.

5 The Xerox rule essentially says that
6 IP is special in some sense. Now, this is a view
7 that I think contains some assumptions that are
8 interesting and I want to talk about just for a
9 moment. The agency's IP guidelines don't say
10 anything definitively, but they do have some
11 portents.

12 It's been noted many times that the
13 IP guidelines essentially say that intellectual
14 property is property. Well, property, the right
15 to exclude incident to other forms of property
16 doesn't give you per se immunity from a refusal
17 to deal liability. Well, why might the right to
18 exclude for IP be different?

19 Well, there's a couple of arguments.
20 First of all, it's the only right. Your right
21 granted in the patent act is the right to
22 exclude. There are other rights incident I

1 suppose, the right to transfer that patent to
2 your heir or to an assign. But the right to
3 exclude is really the key right.

4 As well the right to exclude is said
5 to be the basis for the incentive to innovation.

6 That is what Congress was really getting at ination.

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1 should be imposed on judges that if you are going
2 to say something in Latin, don't say it, because
3 what's been said here doesn't say anything about
4 the extent to which the patent laws modify the
5 antitrust laws in this particular area.

6 To the extent that the patent laws
7 and the antitrust laws relate to the same subject
8 matter, the Supreme Court says the patent laws
9 modify the antitrust laws to that extent or as
10 far as they go. Well, how far do they go? How
11 far does the right to exclude go?

12 The Supreme Court has merely raised
13 the question and hasn't given any kind of an
14 answer. One way of looking at this is laws
15 *in pari materia*, as the Supreme Court said
16 generally, should be harmonized.

17 There's a canon of construction that
18 says they should be harmonized. And that would
19 suggest -- although mildly because canons of
20 construction point both ways. They point all
21 ways.

22 But it would suggest mildly that to

1 the extent we're worried about the scope of the
2 right to exclude it should basically extend only
3 so far as the right to exclude extends for other
4 forms of property. And that antitrust liability
5 for refusals to deal is quite narrow and, as
6 we'll discuss later, should be retained.

7 Jon also talked a bit about the 1988
8 patent act amendments, the Patent Misuse Reform
9 Act. And this piece of legislation basically
10 removes from misuse liability refusals to deal.

11 The question is whether the additional
12 language misuse or "illegal extension of the
13 patent right" also means that antitrust liability
14 for refusal to deal is removed. Well, a few
15 things can be said about that. One, the
16 Solicitor General's brief pointed out that
17 it's the Patent Misuse Reform Act.

18 It doesn't apply on its face to
19 antitrust. The Solicitor General's brief also

1 too promising as Jon pointed out. There are not
2 too many recent cases. It's been -- the doctrine
3 itself has been picked apart pretty thoroughly.

4 But there is refusal to deal liability
5 unrelated to essential facilities that focuses on
6 the conduct at issue and asks whether, first of
7 all, a licensor or a property owner generally has
8 monopoly power and whether the conduct that's
9 being examined involves some sacrifice of profit
10 that would otherwise be available to a lawful
11 monopolist or to a monopolist, period, through
12 exercise of ordinary monopoly pricing.

13 The idea essentially is that a

1 this test focuses on as one prong the promise of
2 recoupment later. But that element of recoupment
3 is not always articulated in the test. The test
4 is profit sacrifice explainable only really
5 through its effect on competition.

6 A couple of things to say about this
7 test. First of all, it's narrow. The plaintiff
8 has to show that the defendant has monopoly power
9 in some relevant market. And the plaintiff has
10 to prove profit sacrifice in the particular way
11 that the test articulates which is a fairly
12 difficult thing to do.

13 It was done in the Microsoft case, but
14 it won't be done I don't think that often. This
15 raises the issue now of remedies. If you're
16 going to have refusal to deal liability based on
17 this narrow test if you find a refusal to deal
18 violates the test, what do you do about it?

19 That's a difficult question because
20 there is no prescription in the antitrust law
21 against charging a monopoly rent. But a remedy
22 would ordinarily involve a compulsory license of

1 some kind in order to license. And that gets a
2 District Court or some other Court into the
3 business of regulating the price of a license.

4 Well, one possibility is that if there
5 is a course of licensing with other licensees who
6 seem fairly similar to the would be licensee, you
7 could essentially impose a license on similar
8 terms and a similar price.

9 But I think as we are going to hear a
10 bit later, that creates a problem by preventing
11 some efficient price discrimination. This is a
12 tough issue. I think we'll talk a bit more about
13 this.

14 But there's one possible approach
15 which is to allow -- to delay remedies and to try
16 to get parties to bargain, as has been put in the
17 shadow of the liability finding. That may be one
18 way to try to set a price, not a perfect way, but
19 perhaps worth discussion.

1 antitrust liability, is that if it weren't we'd
2 have helpful effects on innovation and the
3 incentive to innovate which is the thing that
4 the patent laws are trying to provoke.

5 The simple rule that more exclusion
6 equals more innovation I think is probably
7 something we can get rid of pretty quickly. And
8 there's been a lot written on this, and there are
9 several reasons to think that there is no simple
10 equivalence between exclusion and innovation.

11 A more exclusionary patent regime of
12 course does potentially raise the incentive for a
13 pioneer. But follow-on technologies which may be
14 very important for the commercial usefulness of a
15 product may be disincentivized if the power of
16 the pioneer to exclude is set too high.

17 That's a relatively narrow concern. A
18 broader concern is whether innovation incentives
19 are sufficiently sensitive at the kinds of
20 margins we're talking about of narrow refusal to
21 deal liability that we can reliably say across
22 industries that there is going to be any

1 significant incentive diminution at all.

2 There's an interesting article that I
3 recommend to you by Ian Ayres and Klemperer in
4 the Michigan Law Review in '99 that helps to make
5 the point about why we might want to consider
6 refusal to deal liability as being potentially
7 helpful and good policy.

8 Ayres and Klemperer coin a term the
9 stationarity intuition which they apply to an
10 idea that small restrictions on the scope of the
11 right to exclude may in fact be good policy
12 because they reduce somewhat the patent holder's
13 profit but reduce deadweight loss by a lot more.

14 And although they don't mention
15 refusal to deal liability as a candidate for
16 carrying their model into effect, I wonder
17 whether it might be.

18 Just a bit to close on what the
19 stationarity intuition is. Under Ayres and
20 Klemperer's model they imagine a small narrowing
21 of the scope of the right to exclude such that
22 the price goes from $P-M$ to P -prime.

1 The right to exclude is somewhat
2 narrowed. And the quantity goes up from Q-M to
3 Q-prime as a result because the monopolist has
4 less power over the price. The profit loss from
5 this small narrowing of the right to exclude is
6 the area B minus the area A. The monopolist
7 loses revenues by a lower price on current sales.

8 The monopolist then gains revenues
9 on additional output. And compare that to the
10 relief from deadweight loss from the same move
11 which is the area described in B plus C which
12 is larger under a lot of different assumptions
13 than -- by a lot than the profit loss.

14 The point that Ayres and Klemperer
15 make is that, over relatively small adjustments
16 to the scope of the right to exclude, social
17 welfare may often go up. The incentive to
18 innovate may be unaffected or it may change a
19 little bit. It's hard to say. But this is a
20 trade-off that we should desire.

21 So to sum up, the argument -- the IP
22 argument that the right to exclude is complete is

1 a 90 percent chance of winning, if you're facing
2 a 10 percent chance of \$200 million in liability
3 and you can settle the case for \$10 million, you
4 should settle the case for \$10 million. I think
5 the plaintiffs' bar recognizes that as well. So
6 it's out there.

7 HEWITT PATE: Other comments? If not,
8 Professor Klein?

9 BENJAMIN KLEIN: I think you're right
10 that these cases have to do with ISOs. But the
11 question I would like to ask -- and I'm obviously
12 making a comment by asking this question -- is
13 let's assume that we have the same fact pattern
14 except there were no ISOs.

15 Let's assume that a manufacturer of
16 equipment had a warranty which included all
17 service when they started. So as an economic
18 matter, we really have the same situation, that
19 consumers cannot buy service from anybody other
20 than the equipment manufacturer.

21 I'd like to ask the panel or anybody
22 in the audience whether they would think -- my

1 reading of the law is that there basically would
2 be no antitrust problem with that.

3 GREG WERDEN: That's probably a
4 minority view. Most antitrust lawyers say
5 it's a tie. I've asked them the question.

6 BENJAMIN KLEIN: Okay. Let me hear
7 a case that has to do with that where a firm
8 clearly doesn't have market power in the
9 precontract market like Kodak or Xerox or anybody
10 else. To show an illegal tie obviously you need
11 market power in the tying good market.

12 I maintain that you would never go
13 down the road that we've gone down in this case,
14 not just because we don't have people to bring
15 the case that have been alleged to be hurt, the
16 ISOs, but because it would not fit into the
17 category -- in the usual category of an illegal
18 tie.

19 And it certainly -- I think what is
20 basically involved in these cases is -- at least
21 initially in terms of the Supreme Court case is
22 a holdup, that you need a change in the policy

1 where ISOs are put out of business.

2 HEWITT PATE: Carl?

3 CARL SHAPIRO: I've been involved
4 myself in a number of these ISO cases: Kodak,
5 Siemens, Verian Equipment. And I think there is
6 a common fact pattern that is very attractive to
7 private plaintiffs. The ISOs are smaller. They
8 tend to be appealing to the Jury as opposed to a
9 large corporate defendant.

10 There is this notion of these separate
11 markets, which they probably are separate
12 markets, a various parts market versus a service
13 market. The patent -- the IP is all in the parts
14 area.

15 And a number of these companies
16 have for whatever reason adopted policies or
17 strategies where they are taking a number of
18 their profits through the labor mark-up rather
19 than just the parts. So it makes it attractive
20 for service people to leave, to try to set up
21 their own business, and then they need the parts.

22 So there's kind of a complex of

1 situations here, and of course all following
2 the Supreme Court's '91 decision which opens up,
3 look, this is an area that looks like tying is
4 a real possibility here.

5 It looks like after-market power could
6 be real. And of course the Jury can understand.
7 Hey, I want to get my car serviced and I don't
8 want to pay the dealers the high prices for the
9 parts. So there are a lot of components here.

10 But I think, you know, a lot of that
11 has been driven by notions of tying and leverage
12 which is somewhat distinct from the core issue
13 before us today which is simply unilateral
14 refusal to deal.

15 And one of the interesting things
16 about the Kodak case is after it was remanded
17 as a tying case it transformed into a total
18 unilateral refusal to deal case once the tying
19 claims were dropped. But still of course the
20 plaintiffs prevailed there.

21 HEWITT PATE: Well, in CSU itself
22 the reservation is made of the question of a

1 unilateral refusal to deal that goes beyond
2 the statutory grant.

3 I wonder if in the unilateral
4 blanket refusal context any of the panelists
5 have comments on what it means to go beyond the
6 statutory grant. That seems to be a key question
7 here.

8 CHRIS SPRIGMAN: Well, there are
9 a couple of possibilities. The beyond the
10 statutory grant language suggests I think what
11 the Xerox opinion later makes clear, that the
12 Xerox Court feels that the right to exclude is
13 complete.

14 And so it only makes sense to have
15 antitrust liability for refusals to deal that
16 have some effect outside the statutory grant.

17 Now, I think for antitrust purposes
18 that would mean in some other relevant market or
19 a refusal to deal that has innovation effects
20 that would prevent competition at some time when
21 the relevant IP has expired.

22 I think that's another possibility.

1 And that sounds a lot like, for example, what
2 you see in some of the misuse cases that concern
3 grantbacks. But very little was articulated to
4 specify what the Court meant. So that's by way
5 of a guess.

6 JONATHAN GLEKLEN: I actually -- I
7 have a different view. I think what the Federal
8 Circuit means by the statutory grant is the right
9 to make, use, or sell an item that is within the
10 claims of the patent.

11 So if you've done nothing more
12 than refuse to allow others to make, use, sell,
13 import, offer for sale something that is within
14 the claims of the patent, you are not beyond the
15 statutory grant.

16 There is actually a case. It's an old
17 Tenth Circuit case which says you have the right
18 to prevent others from making, using, selling.
19 But what you can't do is make a contract that
20 goes beyond that or that conditions that.

21 So really tying is outside the
22 statutory grant because you are doing something

1 more than exercising the rights granted by the
2 patent. Price fixing is beyond the statutory
3 grant.

4 But if you just say you can't make,
5 use, or sell something that infringes the claims,
6 I think you're within the statutory grant though
7 I will concede that the Federal Circuit doesn't
8 say that. I just think that's what they must
9 have meant.

10 DOUGLAS MELAMED: This is anticipating
11 what I'll be saying later. A lot of the
12 discussion we have heard and will hear has to
13 do with the likelihood that a unilateral refusal
14 to deal might be anticompetitive.

15 That in large part raises the issue
16 of the so-called one monopoly profit problem
17 and a variety of other problems.

18 I'm in the camp of those who think
19 that a unilateral refusal to deal is rarely
20 anticompetitive in an antitrust sense, although
21 I think it's clear from the literature and I
22 think it's clear from cases that there are

1 situations in which a unilateral refusal to
2 deal can indeed be anticompetitive.

3 The question is not whether
4 unilateral refusals to deal are likely or
5 unlikely to be anticompetitive; it seems to me
6 whether intellectual property should be treated
7 differently from other things that one might
8 refuse to deal.

9 I think this issue of within the
10 statutory grant demonstrates the difficulty of
11 going down the formalistic path of trying to draw
12 these kinds of lines. I don't know what that
13 means.

14 Surely it wouldn't strike me as
15 sensible to say that if you are in a leveraging
16 situation you can state a claim that is not
17 immune from the antitrust laws.

18 But if, for example, you are in a
19 Microsoft situation and Microsoft had chosen to
20 do in Netscape simply by not disclosing its APIs
21 to them claiming they were copyrighted, that
22 that would somehow be immune from antitrust

1 lawfully obtained by skilled foresight in
2 industry, in antitrust parlance, or by the
3 intellectual property that you owned in
4 intellectual property parlance.

5 And I think that must be the intuition
6 behind that kind of language which doesn't
7 otherwise make much sense if you try to translate
8 it into the formalistic question of what is the
9 scope of the patent and what market does the
10 patent give you rights in and those kinds of
11 questions.

12 HEWITT PATE: If that's the test, is
13 there implicit a requirement of recoupment, do
14 you think, a requirement that the plaintiff show
15 recoupment as likely?

16 DOUGLAS MELAMED: Yes, in theory.
17 Now, whether there is an appropriate area in the
18 law to presume recoupment without having to prove
19 it is a second order question. But in theory,
20 absolutely.

21 HEWITT PATE: Jeff, do you have a
22 comment?

1 JEFF MACKIE-MASON: Yeah. This is
2 probably mostly a question to Jonathan. It's
3 really a puzzle I've had that comes from the
4 issue about things being within the statutory
5 grant. As an economist I've been trying for some
6 years to figure out what that means, and I know
7 I'm not there yet.

8 I wanted to raise a couple of
9 hypotheticals, one of which -- well, both of
10 which probably sound a bit farfetched but as far
11 as I can tell are not ruled out by at least
12 Jonathan's and many people's interpretation of
13 the Fed. Circuit in Xerox.

14 And that is it sort of -- it starts
15 with Kodak because one of the things the Ninth
16 Circuit had to deal with in Kodak, which was a
17 puzzling situation for it I think and it's one of
18 the reasons that Kodak is different in some ways
19 from the other cases, is that very few of the
20 parts that were involved in Kodak actually had
21 patents.

22 There are arguments about that. But

1 something like 65 to 100 out of 10,000 parts had
2 patents. And there was never any allegation that
3 those -- well, I shouldn't say that, and Carl
4 will argue with me.

5 But the case did not revolve around
6 the criticality of those parts the way it did in
7 Xerox where the parties basically admitted that
8 those parts were the crucial parts. So, you
9 know, a question arises: Is it really the
10 intellectual property that's being used or
11 protected?

12 I mean after all the ISOs weren't
13 making parts in competition. They were really
14 just acting as agents for the customers and
15 installing parts on behalf of customers.

16 So the hypothetical I want to raise
17 and just hear reaction from Jonathan or anybody
18 else is what if Xerox patented the design on
19 a washer, Xerox or anybody, and attached that
20 washer to all of its other parts, just glued it
21 on, had no functional use, but they attached it?

22 Does that now mean that all of their

1 parts are protected by patent and they don't have

1 to me. Or somebody did the hypo, you know,
2 I inscribe a short, original poem on each of
3 my parts.

4 Your refusal to sell -- you have
5 no good reason for linking the stupid patented
6 washer to the valuable yet unpatented part,
7 though I'd also wonder whether you could
8 really have market power in that part that's
9 of significance to the antitrust law because
10 somebody else could design the part without
11 the stupid patented washer.

12 HEWITT PATE: I suppose by using the
13 washer you meant to make it a stupid washer. I'm
14 not sure if that's true.

15 But if it is true, I guess the Baird
16 case I believe it is from the Federal Circuit
17 suggests that, you know, a change in design that
18 really doesn't have any function may not be quite
19 the same thing as a really valuable washer that
20 got added to a lot of other parts that were, you
21 know, not patented.

22 JEFF MACKIE-MASON: Yeah. I did mean

1 it to be a stupid washer. And obviously there's
2 possibly some answer although I shudder at the
3 thought of trying to litigate and determine
4 whether particular design decisions -- I mean it
5 actually isn't that stupid a hypothetical in the
6 sense that in many of these cases it wasn't the
7 whole device or unit that was patented.

8 It was some piece of design or process
9 within the device. And whether or not that was
10 essential is unclear. And I think actually,
11 Jonathan, to have the market power despite the
12 stupid washer probably is there. Kodak did in
13 its parts, and most of those had no patents
14 involved.

15 And for that matter most of Xerox's
16 parts didn't either, and they probably had market
17 power in those parts even though those weren't
18 the ones that were critical to the technicians.

19 HEWITT PATE: Other comments on the
20 hypothetical?

21 BENJAMIN KLEIN: The part, the stupid
22 washer may serve no technological function. But

1 it may serve a legitimate economic function that
2 it permits the IP holder to efficiently collect
3 for the value of the IP which is something that
4 could explain what happened in Baird.

5 I mean it might be very difficult for
6 an IP holder, for example, somebody that has --
7 I forgot what that case was, some kind of biopsy
8 gun or something.

9 And they were clearly using the
10 needles as a way

- 1 gun that they should be allowed to try to collect
- 2 for the IP in any way that they find economically

1 HEWITT PATE: We're going to resume
2 the morning session now with a presentation by
3 Professors Klein and Wiley.

4 JOHN WILEY: Good morning. I'm John
5 Wiley. With me is Ben Klein. We're from UCLA,
6 and we're very pleased to be here. We're here
7 to talk about this conflict that Hugh Pate
8 introduced and that the speakers and discussants
9 have covered in quite a bit of detail so far.

10 This pair of cases is conventionally
11 thought of as an antitrust/intellectual property
12 conflict, the conflict between the Kodak case
13 which was obviously a plaintiffs' judgment for
14 some number of dozens of millions of dollars.

15 It wasn't a colossal case, but a few
16 dozen million here, a few dozen million there,
17 pretty soon we're talking about real money.
18 There was an intellectual property defense
19 attempted by Kodak, the defendant, and it
20 flopped. The Ninth Circuit said it was pretext.

21 So in contrast to that case is the
22 Xerox decision. And of course that was a

1 is all the more intense.

2 Now, our position is that to consider
3 these cases as an intellectual property antitrust
4 conflict is to misperceive the key issue. It
5 is indeed true that most people talk about the
6 antitrust intellectual property conflict in these
7 cases. But we think these two cases are actually
8 about something else entirely.

9 To emphasize the intellectual property
10 angle we say is the wrong perspective. Rather
11 we say that in fact the two cases are in a
12 profound way about antitrust treatment of price
13 discrimination. Now, you can't learn that from
14 looking at the cases. The cases never talk about
15 price discrimination.

16 And there's a reason for that. The
17 lawyers in the case never talked about price
18 discrimination, and there's a reason for that.
19 The reason for that is mistaken antitrust
20 hostility to price discrimination.

21 Antitrust cases in the past have
22 damned price discrimination as a legitimate

1 business justification in dicta, and it is those
2 cases we say that are to blame for the confusion
3 in this area.

4 So our basic position is that the real
5 problem in this area is not one of intellectual
6 property policy. It is this old antitrust dicta
7 about price discrimination. And that's what
8 really needs to be fixed.

9 Price discrimination or metering,
10 as it's been called this morning, is often a
11 reasonable and entirely procompetitive way to
12 collect for the use of valuable property, any
13 kind of property, not just intellectual property.

14 So really these cases we think are
15 about something other than what the doctrine says
16 they are about. So we would like to turn to the
17 basic economics of what's going on in these cases
18 to understand the real conflict.

19 And for this I'm going to ask Ben
20 Klein to talk about the economics of price
21 discrimination and the practices in these cases.

22 BENJAMIN KLEIN: I guess you've heard

1 my story already about how refusals to deal
2 enable a firm to price discriminate. And price
3 discrimination is used here as an economist uses
4 price discrimination.

5 This is not in the Robinson Patman
6 sense, but in the economic sense just that there
7 are different customers or customer groups.
8 And you can earn different economic margins by
9 charging differential prices relative to the
10 costs of servicing those two groups.

11 And the usual economic analysis
12 is that the people that use a product more
13 intensively, the higher service users, probably
14 have a greater willingness to pay. They have
15 a greater all or nothing value that they are
16 willing to place on the package. So you want to
17 charge the more intensive users a higher price.

18 And one way to separate out the users
19 and charge the more intensive users a higher
20 price is to collect it on an after-market product
21 like the service.

22 So this is just, you know, the razor

1 blade strategy. And the interesting economic
2 question is if you want to meter after-market
3 demand why don't you just put it on the parts.

4 Put an up-charge on the parts and
5 therefore, the people that use the equipment more
6 intensively and need more replacement parts are
7 the ones that will end up paying a higher price.
8 And I guess there's nothing more on that slide.

9 But the reason that it may not be
10 profitable to put it on the parts, put the
11 up-charge on the parts as an efficient metering
12 device, is that the firm may want to price
13 discriminate across consumers in a number of
14 other ways, like by the type of service they
15 purchase, whether they want, you know, repair
16 service within 3 hours or whether they are
17 willing to wait 24 or 48 hours.

18 You also may not to charge large
19 users that service their machines themselves very
20 low prices because those are probably the most
21 knowledgeable customers and probably have the
22 most elastic demands. And it seems like there's

1 evidence in these cases that in fact the
2 self-service prices were relatively low.

3 And therefore you don't want
4 to collect it as an up-charge on the parts
5 price because then you would be charging the
6 self-service customers too high a package
7 price. And in addition there's some variable
8 proportions. I hope I don't use too much jargon
9 here.

10 But there is a trade-off between parts
11 and service that if you jack up the price of the
12 parts people may just service the machine more
13 intensively and not need to repair it and replace
14 the parts as frequently.

15 So for all these reasons it may be
16 economically efficient to collect it in the
17 after-market for the service. Now, the problem,
18 John and I say, is that this is okay except in
19 the case law -- and it's not really that
20 important in the case law. There are a few
21 dicta.

22 But it's more a major part of

1 antitrust scholarship that price discrimination
2 has a bad rap. And in particular there are two
3 characteristics of price discrimination that are
4 considered bad: One -- and this is by far the
5 most important that messes things up -- that
6 price discrimination is evidence of market power.

7 And the best quote we can find for
8 that was in Fortner II where the statement is
9 something like price discrimination implies the
10 existence of power that would not exist in a free
11 market. And the second bad rap is that price
12 discrimination has bad economic effects.

13 And this one, it's more difficult to
14 find in the case record, but we found something
15 in Jefferson Parish that's in our paper that
16 talks about the social costs of permitting a
17 monopolist.

18 It assumes the first thing, and
19 then it says if you let a monopolist price
20 discriminate you increase the social cost
21 associated with that. So let's go through
22 these things one at a time.

1 The first bad rap, that price
2 discrimination is evidence of market power,
3 it's pretty obvious to an economist that price
4 discrimination is not evidence of market power.
5 It's only if you think of competition as the
6 perfectly competitive benchmark.

7 But once you have differentiated
8 products, just about every firm can price
9 discriminate. And every firm has a negatively
10 sloped demand curve, and they can therefore
11 possibly increase their profits by price
12 discriminating. And I always -- I never
13 know what example to give my classes.

14 I mean this -- price discrimination is
15 all pervasive, and really just about every firm
16 does it. I usually talk about manufacturers of
17 products in a grocery store where they have very
18 small market share. Some of these people are
19 giving out coupons and giving discounts to some
20 people and not discounts to others.

21 But clearly people are not price
22 takers like in the textbook economic model of,

1 you know, the wheat farmer. But probably the
2 best example is -- I decided is -- John and I,
3 that we have negatively sloped demand curves, and
4 we can price discriminate. In fact some people
5 might say we're doing that today.

6 But I don't have to worry about if
7 I increase my price a dollar for my consulting
8 services that my demand goes to zero. And if
9 I want to, I do have the ability to price
10 discriminate.

11 And the key thing here, the key
12 analytical point is that the ability to affect
13 your own price, that is the ability to have
14 individual firm pricing discretion over what
15 you're going to charge, does not imply the
16 ability to affect the market price.

17 Even though I could figure out
18 what consulting rate I'm going to charge for
19 my services and if I want to I can price
20 discriminate, I obviously have no ability to
21 impact the market for consulting services. I
22 have a trivial market share. And anything I do

1 will have absolutely no effect in that market.

2 So maybe I should -- I thought there
3 was something else on that slide. Let me just
4 say before I go on to bad rap two that this is
5 the problem that causes most of the difficulty,
6 just being able to assume that if you see price
7 discrimination it's evidence of market power.

8 And it's not only why firms can't use
9 a metering defense as an efficiency rationale for
10 how to collect for their intellectual property
11 and other property, but it actually is perverse.
12 It goes the other way.

13 And when the Kodak case went back on
14 remand to trial, actually there was no longer
15 this assumption that the Supreme Court had that
16 there was no precontract market power. And there
17 was a whole -- Jeff can talk about it because he
18 was there if he remembers the facts.

19 But there was a whole debate about
20 when Kodak had market power. And the plaintiff
21 ISOs actually used the fact that Kodak was price
22 discriminating as evidence that they had market

1 power, not this holdup condition that the Supreme
2 Court was concerned about, but actual precontract
3 market power because they were charging customers
4 different prices.

5 And the defense had a very difficult
6 time. The example that they finally used to show
7 that market -- that price discrimination is not
8 evidence of market power is they used movie
9 ticket pricing. I'm not sure that was the best
10 example. But that was the example they used.

11 They said, look, there's senior
12 discounts. There's children's prices. There's
13 all this other stuff. But it's -- you're going
14 up -- you're clearly going uphill if you want to
15 say that price discrimination is part of a normal
16 competitive process even though we think it is.

17 The second problem about price
18 discrimination is that price discrimination
19 implies economic cost. And price discrimination
20 clearly does not necessarily have social costs.
21 Price discrimination in fact can often be good
22 for consumers. There's this casual notion that

1 price discrimination is good for the firm.

2 It increases its profitability.

3 But it's not good for the public. And that is
4 generally not true as a general proposition. And
5 there are plenty of circumstances where the total
6 quantity goes up or doesn't change. And in
7 particular in many circumstances there can
8 be an increase in the user base.

9 This is a way -- without price
10 discrimination some markets and some consumers
11 may not be served at all. By lowering the
12 equipment price low intensity users who would not
13 purchase the package if the equipment were priced
14 higher get the opportunity to use it.

15 So it increases the user base. And
16 the usual effect because it increases the firm's
17 profitability is it increases the incentive for
18 the firm to innovate.

19 So the general proposition that
20 there's this trade-off between the short
21 run or static inefficiencies when you have
22 price discrimination against these long run

1 efficiencies increasing the incentives to
2 invest are not necessarily there. And I guess
3 I should -- how many more slides do we have?

4 Let me just say one more thing.
5 There are some examples where a refusal to deal
6 is not just an efficient way to collect for
7 your intellectual property, and it may have
8 anticompetitive effects.

9 I personally believe that those
10 cases are extremely rare, the cases where the
11 firm is using it to create a barrier to entry, to
12 maintain the monopoly, or to leverage it into a
13 market where there are very large economies of
14 scale like in the Winston model.

15 But they certainly -- those models
16 certainly don't apply to these ISO cases. And I
17 think it's easy to screen out those cases by just
18 having some kind of market share screen for the
19 firms.

20 Then it becomes a question about how
21 do you define a relevant market and do you want
22 to say that Kodak has a monopoly on the sale

1 of Kodak copiers, or do you want to define a
2 reasonable market. John, do you want to finish?

3 JOHN WILEY: So the key question here
4 today is really: What should the government do?
5 What should the FTC, what should the Antitrust
6 Division do about this conflict in the case law?

7 And we say the following: First of
8 all, let's be clear about what's going on in
9 these two important cases.

10 They are cases that are really about
11 price discrimination where Kodak, where Xerox are
12 selling machines at a relatively low price and
13 then collecting additional fees based on service
14 and parts so that high intensity users pay more,
15 low intensity users pay less. The cases are
16 about price discrimination.

17 And the antitrust policy that is
18 hostile to price discrimination forced Kodak to
19 submerge the true explanation for its conduct
20 and never to be candid about what it was really
21 doing. To be candid that, oh, yes, we're just
22 price discriminating would be to invite virtually

1 a stipulation of liability.

2 So we proceed immediately to the
3 question of, okay, now that you have told us what
4 you are doing, the only issue is how many dozens
5 of millions of dollars will you have to pay for
6 it. That's mistaken antitrust policy.

7 So the correct antitrust policy would
8 recognize that price discrimination is okay, that
9 it's a valid business justification for a refusal
10 to deal. Now, if we acknowledge that's part of
11 the normal competitive process that you as
12 lawyers are price discriminating, you don't
13 have a single rack rate necessarily.

14 Well, maybe you do in your firm. But
15 you know of other firms where the same lawyer may

19e a single rack dollarae acmonon is okaypingttivr

2sinesA TjdiscrT* raebadon is okaypingttivrck dol

16 be billing one 2eal

1 need help in this area.

2 And it would be appropriate for the
3 high prestige federal antitrust cops to intervene
4 appropriately, to look for cases that come up
5 like this in the future, and to intervene as
6 the Federal Government often does to try to
7 eventually get the Supreme Court to change these
8 Fortner and Jefferson Parish dicta that drive the
9 true explanation for these cases into hiding. We
10 would all be the better. Thank you very much.

11 (Applause.)

12 HEWITT PATE: We're going to continue
13 with Professor Arora's presentation. I'll throw
14 something out not for discussion but maybe to
15 think about after he concludes, which is whether
16 the problem John and Benjamin have discussed
17 doesn't go beyond antitrust.

18 It seems to me that as a matter of
19 patent law -- I think of the Salt case -- there
20 may be problems with using metering from a misuse
21 perspective.

22 Or even over time one form of price

1 discrimination might be to allow those who don't
2 have enough money to pay the royalty sought by
3 the patent holder up front, but they could do so
4 over a long period of time that extended beyond
5 the patent term.

6 The Supreme Court makes clear that as

1 an economic commodity, and specifically as an
2 economically tradeable commodity.

3 So I'm interested in when
4 technologies get traded, when they get bought
5 and sold, when and under what conditions and with
6 what consequences. And so I'll tell you a little
7 bit about just a very brief comment on that.

8 That leads to sort of the second part
9 which is from my perspective it's natural to
10 think of intellectual property as any other type
11 of property. And I couldn't agree with Chris
12 more when he says, look, the right to exclude
13 is implicit in all property.

14 There's nothing particularly different
15 about intellectual property. However, from a
16 transaction perspective, so if you think about
17 doing something about a refusal to license, there
18 are some interesting differences. And Hewitt
19 Pate mentioned some of those. And I'll talk a
20 little bit about that.

21 So there's some good news, bad news
22 from the second bullet. The third bullet I guess

1 you should put down to my naivete which is sort
2 of fools rushing in where angels fear to tread
3 which is I'm actually going to propose something
4 that works or might work and see whether -- how
5 many of you think this is a sensible proposal.

6 As I said, I guess I've got nothing to
7 lose because I have no particular stake here. So
8 I believe it was Jonathan who said that IP is not
9 used in that market. And that's sort of partly
10 true. And many people sort of make claims of
11 this kind, that there's no market for technology
12 or no market for innovation.

1 30 and 50 billion dollars per year.

2 And our data, I should point out, are
3 roughly 1990 to 1996 or '97. And obviously you
4 can quibble about how one does it. But as order
5 of magnitude these numbers I think are pretty
6 sensible. And so from my perspective, I think of
7 these trades as socially beneficial. They avoid
8 duplicate R & D.

9 They promote diffusion of technology.
10 They promote specialization and enhance the rate
11 of innovation. And so in that sense I have a
12 pro-IP bias, I think, of crisp IP. I've written
13 a strong -- and I don't want to be held to that.

14 But certainly crisp, well defined
15 intellectual property is good. I'm a firm
16 believer in that. And a flip side, a sort of
17 benefit of market for technology is that some of
18 the practical problems of pricing get easier when
19 there is a market for this stuff.

20 So as I said, I think of IP as any
21 other type of property right. And in passing
22 I should mention that if you have markets for

1 technology, then you can have market power in
2 those markets. And sometimes it's taken as
3 axiomatic that because you have a patent you're
4 going to have a monopoly.

5 I think that's highly overstated.
6 The typical case is you have substitutes. So
7 Professor Klein talked about differentiated
8 products, and I think that's a good way to think
9 about the market for technology.

10 And I think the federal agencies have
11 been properly watchful about accumulation of
12 market power. And I think they are to be
13 commended for that.

14 So this perspective then says I'm
15 mischaracterizing the IP against antitrust
16 challenge or sort of carving out separate things,
17 separate ways of looking at IP I find actually
18 disturbing.

19 And I find it particularly disturbing
20 because we're going to soon live in a world where
21 there's going to be IP sitting in lots of places.
22 There's going to be embedded software in all

1 kinds of things that you probably don't think of.

2 And to carve out separately that goods

3 are going to be treated one way and IP is going

4 to be treated a different way is just going to

5 make I think a mess.

6 Now, that said, I think IP is

7 different partly because it's not clear what the

8 scope of the property is and because it often has

9 to be bundled with other stuff. And this is -- I
10 guess my take -- well, let me back up.

11 There are two outstanding examples of

12 compulsory licensing in U.S. history. They both

13 happened after wars, and they both dealt with

14 German patents and a variety of German industrial

15 property.

16 And essentially German patents were

17 taken over and made available to U.S. firms.

18 There is a lot to be learned from that, and

19 that's not been sufficiently studied.

20 But one interesting thing was U.S.

21 firms found it extraordinarily hard to make use

22 of the patents. It was very, very difficult.

1 Partly this had to do with German patenting
2 practices. But part of it was you need a lot of
3 know-how and this know-how had to be gotten in
4 various ways.

5 And there are lots of examples of how
6 U.S. firms went about trying to get know-how.
7 And maybe at a different time I can tell you some
8 interesting stories about the use of something
9 that looked like Super 301 except in reverse, the
10 U.S. trying to get intellectual property by
11 threatening trade sanctions.

12 Anyway, so what does this mean? Well,
13 what this means is compulsory licensing is going
14 to be tough. How do you ensure that the know-how
15 is being transferred? That's going to be a hard
16 problem.

17 Second, I think policy has to be --
18 has to allow flexibility in contracts. If we
19 want efficient transfer of technology, the
20 know-how has to come along with the intellectual
21 property. And I've done some research on this
22 and others have too.

1 But basically bundling is one way, not
2 the only way, but it's one way in which you can
3 accomplish the successful transfer of know-how
4 which is not patented and subject to sort of --
5 there's a greater danger of opportunistic
6 behavior or of the buyer sort of not behaving
7 properly and so on.

8 So I guess in that sense this would
9 say, well, we should use compulsory licensing or
10 something that looks like that, you know, with a
11 great deal of caution because it's going to be
12 hard.

13 There are possibly related issues
14 where if you compel people to license and this is
15 anticipated they may hold more of the property
16 which is not patented in the form of know-how on
17 the chance that you have a greater likelihood of
18 protecting that.

19 So let me move to the last part which
20 is I suppose both -- well, this is a part that I
21 have most fun doing because it's completely new.
22 And this is a part that may I suspect prove to

1 be -- well, I'll leave you to decide whether it's
2 useful or not.

3 So I'm going to just make some
4 premises. There are cases in which refusal to
5 deal may reduce social welfare. There is not
6 going to be any special immunity just because a
7 thing is patented.

8 Incidentally, as I read the evidence
9 there seem to be sort of separate treatments of
10 copyrights and patents which on one ground can be
11 defended that a patent is sort of a hard right.
12 You have a greater threshold to cross.

13 But since Mr. Polk is here from
14 the PTO, it's worth pointing out that at least
15 according to some estimates the probability
16 that a patent will be granted is in excess of
17 90 percent. And if those statements are correct,
18 we're approaching something that looks like a
19 registration system for a patent.

20 And I confess the Patent Office's
21 greater drive to be more customer friendly
22 worries me even more because I'm not sure they

1 have correctly identified their customer. It is
2 not the guys applying for the patent alone.

3 Anyway, that's a -- I couldn't resist
4 since Mr. Polk is here. So I'm not even going to
5 try to give this -- ground this in any kind of
6 legal doctrine or principle, and less forgivably
7 not even in a well worked out theory of
8 economics.

9 Basically I guess the idea is if --
10 what we are worried about with this refusal to
11 license is, look, if we impose this there is
12 going to be reduced incentive to innovate versus
13 some sort of benefit.

14 One way of thinking about this is we
15 should try to have some sort of commensurability
16 or proportionality between -- we should have some
17 sort of proportionality. And I guess one way to
18 begin is by saying, so why is the license needed.

19 My perspective suggests that there
20 are always substitutes. Maybe not the best ones;
21 maybe they are not perfect substitutes. But they
22 are usually pretty good substitutes.

1 Unless we have something that's --
2 well, even take the strongest patents you can
3 think of, which is a composition of matter patent
4 in chemicals. So DuPont had nylon. Well,
5 IG Farben figured out a slightly different
6 version which is perlon, perfectly valid patent.

7 So that then leads to the question, so
8 why is the guy asking for a license in the first
9 place; why doesn't he just try to invent around?
10 There could be two reasons for this, or at least
11 two reasons.

12 One says, look, the technology is
13 really superior. The alternatives are really
14 inferior. And so in that sense I think there's
15 no question. If a technology is really superior,
16 you probably don't want to compel a license. The
17 patent holder has truly sort of discovered
18 something useful.

19 And I'll try to explain that a little
20 bit more. The second reason could be that what
21 the patent holder is trying to do is leverage or
22 gain market power in a related market by

1 exploiting some sort of standard.

2 And here I'm sort of building on a
3 very interesting article by Robert Merges. It's
4 called Who Owns the Charles River Bridge, and you
5 can get it off his website at the UC-Berkeley law
6 school.

7 So this part, at least the idea
8 of leveraging I've learned from reading that
9 article. And the principle I want to try to
10 implement is that the social benefit of the
11 innovation should be commensurate with the
12 private benefit.

13 So we want to let the patent holder
14 get rents from this market. But you should not
15 be allowed to leverage, quote, a very small
16 property right into a very large market.

17 And let me quickly tell you how to do
18 it and I can tell you the problems with it as
19 well. So the basic idea is what you think about
20 doing is you take the IP and you spin it off.

21 So you take the IP that's been refused
22 license, take it out as a separate firm and ask

1 yourself what would be the value of the spinoff.
2 And I'm going to propose that that's at least a
3 first reasonable order approximation of what the
4 social value of this innovation is.

5 And if there is a big difference
6 between the estimated value of the spin-off and
7 the market that's being sought to be leveraged or
8 where this license is being refused, then you
9 say, well, why is this? Is there a general
10 complementarity, or is there something else
11 going on?

12 And if you can not find -- so this is
13 sort of like the stupid washer example. If there
14 is no sort of real reason for the washer to be
15 there, you might sort of look deeper. I'm not
16 claiming that this is the complete test. This is
17 one possible way of implementing this.

18 I'm running out of time. So let me
19 quickly just tell you what are the objections to
20 this because I believe the best defense is to
21 admit up front what the problems are. Yes, it
22 does -- it will impair incentives to innovate.

1 Yes, it is in conflict with the
2 doctrine that patents contemplate the right to
3 exclude. And, yes, it does run into the valid
4 objection that this method ignores legitimate
5 complementarities.

6 And, yes, there is the problem of
7 the difference between the patent scope and the
8 market scope. And, yes, it's not going to be
9 easy to do.

10 But this brings me back to my starting
11 point. When markets for technology -- if they
12 continue to grow, it won't be as difficult as it
13 might otherwise be. Thank you very much.

14 (Applause.)

15 HEWITT PATE: Comments or questions on
16 these presentations? I guess personal privilege
17 for Mr. Polk here.

18 EDWARD POLK: I thought I may go
19 unscathed here since we were talking about
20 licensing. But just to make sure we are clear,
21 the approval rate for the Patent Office is about
22 60 percent which is pretty much in line with

1 other countries.

2 I know an earlier speaker had
3 suggested 90 percent, but if I could draw
4 from Mr. Bush there with his fuzzy math, the
5 90 percent there.

6 Another point that Mr. Arora raised
7 which I think is a good point there is it seems
8 as far as the patent, the difference between the
9 patented property and the other property, it
10 seems that it may be better antitrust policy or
11 even the whole competition that we're looking at.

12 It seems that a lot of folks are
13 saying that there should be somehow an allowing
14 of others to piggyback off of the patented
15 property. And if we're interested in
16 competition, shouldn't we be more interested in
17 allowing companies to design around, or if they
18 think the patent is invalid -- I don't know.

19 Maybe you can answer this. In the
20 Xerox case I didn't see any challenges to the
21 validity of the patent which, you know, that's
22 a way of getting around someone refusing to

1 license; invalidate their patent or go out and
2 make your own product.

3 And if there are any comments you
4 would maybe know the facts of Xerox that would
5 answer it.

6 ASHISH ARORA: Could I just get the --
7 on the numbers, this is an article by Quillan and
8 Webster. And the difference is in how you treat
9 continuations. Anyway, I have no particular
10 expertise. If this is true, the 90 percent is
11 disturbing.

12 JONATHAN GLEKLEN: Just so people
13 know, on the facts of Xerox there is no challenge
14 to the validity of the patents. CSU conceded
15 invalidity and infringement.

16 CHRIS SPRIGMAN: On the issue of
17 piggybacking on others' patents, I take that to
18 be -- to relate to comments I made about the
19 scope of the right to collude and comments that
20 Professor Arora also made.

21 I think it's important to state again
22 what's at stake here between a complete right to

1 exclude and a right to exclude that extends only
2 so far as antitrust liability for refusal to deal
3 begins. This is not a huge difference. I think
4 though it's an important difference.

5 The question is what right to exclude
6 does the statute grant. Well, it's clearly
7 not -- it's not clearly one or the other. And
8 there are good I think reasons to think for
9 efficiency that the right to exclude should be
10 limited at the margin by refusal to deal
11 liability.

12 I think there's also something else
13 that's worth saying. I've heard at a lot of IP
14 conferences among the IP community the right to
15 exclude is talked about in this kind of totemic
16 fashion. What else could it be but the right to
17 exclude? Exclusion is the right.

18 Well, the Founders didn't see it that
19 way. I'm pitching my own articles. But I wrote
20 an article about the Copyright Term Extension Act
21 that you can find on find law.com some weeks ago.

22 And there is a hyperlink to some

- 1 normative significance to the idea of leveraging
- 2 something small into something big. I'm not sure

1 illuminate the question, is defendant using it
2 strategically, not to maximize its value but
3 rather to achieve some anticompetitive or what
4 you would call some recoupment payoff.

5 And that might help identify those
6 instances in which the IP is being exploited in
7 an anticompetitive way.

8 ASHISH ARORA: I agree. That's sort
9 of what I had hoped to do in my slide ten, but
10 never got to it.

11 HEWITT PATE: One of the questions
12 that's been raised is whether the right to
13 exclude ends where the duty to deal under
14 antitrust law begins. Is there anybody who is
15 interested in taking a stab at the general
16 question of when the duty to deal ought to begin?

17 It was suggested to me yesterday in
18 another context that if you look at the cases,
19 essential facility and otherwise, you don't
20 really find liability except where ad l.yu2d1, whether the right tex eIdo

1 harbor territory.

2 On the other hand, you clearly have to
3 have a benchmark. You have to have some way of
4 saying what are the terms on which one might have
5 expected this party to deal; what basis do we
6 have for thinking that dealing might have been
7 profitable and might have been practical and
8 might have been efficient?

9 And so in the absence of some
10 benchmark in the experience of this defendant
11 dealing with somebody, if not the plaintiff,
12 somebody, it probably would be a very unusual
13 case, maybe one like Otter Tail were AT&T
14 required regulatory oversight for the Courts to
15 feel that they had a sufficient benchmark. But
16 that to me is a matter of prudence and
17 expediency, not one of principle.

18 MARK WHITENER: Can I reply to that?
19 That's an interesting point because one of the
20 things that happens I think when you acknowledge
21 that to have a meaningful remedy you need some
22 sort of benchmark is you start affecting behavior

1 simply by stating that rule.

2 So, for example, if an IP owner
3 is making the decision initially whether to
4 integrate vertically or to exploit their IP in a
5 particular area, they are now going to have to
6 take into account the fact that once they are
7 occupying that space under some statements of the
8 legal rule they have taken on greater exposure
9 because now by occupying that space, by making
10 what let's just assume for the moment is an
11 efficient decision to exploit their IP in a
12 particular sphere, or let's say to license some
13 one, pure, non-competing customer, now they have
14 created a benchmark.

15 And so now you have gone from a
16 situation where you might not have had a
17 meaningful remedy to one in which, well, you
18 have created now a standard against which you are
19 going to be held and you are going to be required
20 to license.

21 I just add that my general observation
22 about probably this whole day and picking up on

1 the last two presentations is I think that it's
2 going to be very interesting to hear as the day
3 unfolds who can articulate, you know, a
4 meaningful standard for liability if in some
5 cases there is liability for a unilateral refusal
6 to deal.

7 And a standard that doesn't simply
8 restate the boilerplate of exclusionary conduct
9 but that sets out at least some realistic
10 description of necessary or sufficient
11 conditions, to apply that standard to a refusal,
12 I think it's a very difficult thing to do.

13 I think various people have taken a
14 stab at it. I'm not sure anybody has succeeded.
15 And especially I'm not sure anybody has succeeded
16 without essentially requiring an after the fact
17 assessment of, well, what might have been the
18 profit maximizing behavior for this IP owner
19 when they made the initial decision whether to
20 license, whether to exploit, and how to exploit.

21 JONATHAN GLEKLEN: Two points, both of
22 which are following up on Mark. And I think what

1 he said is exactly right. The first is -- and
2 this came up -- I think it was an FTC
3 investigation of a transaction that Monsanto
4 was doing, basically reacquiring IP that it had
5 formerly licensed.

6 And Dennis Yao concurred and then
7 wrote an article about it. And what he said
8 is you have to be very careful that we don't
9 penalize people for making bad licensing choices
10 and then trying to change their mind, because if
11 you do that it creates huge incentives never to
12 license.

13 If I know that once I license I either
14 can't terminate the license or can't reacquire
15 the licensed IP or that that is going to be a
16 benchmark for what a reasonable person would have

- 1 spinoff to IP Co. or are we trading off
- 2 short-term profits for long-term monopoly profits
- 3 with a recoupment test.

1 HEWITT PATE: Let me go to Chris and
2 then back to Mark.

3 CHRIS SPRIGMAN: Take a quick stab
4 at Mr. Whitener's challenge and also at some
5 comments that John just had. First of all, every
6 case does not go to a Jury. The DOJ just lost a
7 case on market definition on a PI.

8 And it's market definition and market
9 power, in fact monopoly power here is something
10 that is a substantial screen as that experience
11 shows. Plaintiffs are going to have to walk in,
12 and they are going to have to prove up why this
13 IP holder has sufficient power that they should
14 get to a Jury.

15 We're reminded again and again and

1 monopoly profits which it's entitled to reap in
2 return for exclusion which it hopes to exploit in
3 the future and recoup and put itself in a better
4 position.

5 That's a difficult set of issues. But
6 it's worth remembering that that difficult set of
7 issues is not relevant only in the IP context.
8 It's relevant to any refusal to deal case in
9 any context.

10 And it may be the fact that our
11 squeamishness with refusal to deal law in the
12 IP context is reflective of our general
13 squeamishness with respect to refusal to deal
14 law. But, you know, again it's worth
15 considering.

16 If refusal to deal liability is
17 sufficiently narrow, and if a sufficiently narrow
18 constraint on a monopolist's right to exclude is
19 imposed, we may benefit from uncertainty. An
20 imperfect machine may be in our interest.

21 And so the entire conversation may
22 have somewhat of an Alice in Wonderland quality

1 say that there is some theory of exclusion that
2 we apply every day.

3 You know, we've got to get to the
4 hard questions. What is the conduct that's
5 exclusionary? Is it the non-sharing of the
6 property right? Yes or no? What are the
7 justifications in a rule of reason analysis which
8 surely it must be that are taken into account?

9 Is it the desire to achieve a full
10 return on the initial investment in the IP? And
11 then you get to remedy. And I think that issue
12 alone probably is enough to really bog us down
13 for a whole other day.

14 HEWITT PATE: Let me throw out a
15 couple of questions. It seems obvious to look
16 at refusal to deal law where the question was
17 whether the refusal to sell a part was -- where
18 the question is whether that was legitimate.

19 Would it have made a difference do
20 people think if the context had arisen in a more
21 pure patent context, say, that the ISO wished to
22 manufacture a patented part in its own plant and

1 maybe could have done so more cheaply and a
2 refusal to license prevented them from doing that
3 even if there were no question of a refusal to
4 sell a product?

5 Likewise, does it make a difference,
6 as has been suggested, whether know-how or trade
7 secrets would be required to be conveyed in order
8 to make use of the property? Does that make any
9 difference in how the antitrust law ought to view
10 these situations? Well, I got Mark to turn his
11 sign down with that question. All right. Carl?

12 CARL SHAPIRO: I'll just briefly say
13 it seems to me the know-how point is a very good
14 one. In some contexts, as Professor Arora
15 pointed out, the patent may not -- a license to
16 the patent may not be worth much without some
17 hand-holding and other expertise.

18 That just I think reminds me at least
19 how IP is not that much different than other
20 areas where there may be some costs associated
21 with the holder of the rights if there's going to
22 be mandatory -- if these duties exist.

1 As I will say after lunch, I think it
2 is a reason to treat IP like other types and not
3 have these duties in either area.

4 But it's good that -- it's not sort of
5 the pure case of, you know, you just send over a
6 piece of paper that says, fine, you can use this
7 patent; go to the Patent Office and look up the
8 patent and you'll be fine; goodbye. There's more
9 involved, which is what would be true for other
10 types of property often.

11 HEWITT PATE: Other comments? Gail?
12 Other questions that people want to throw out?
13 If not, I'll try to avoid violating the cardinal
14 rule of moderating, which is never make people
15 late for lunch and if possible let them have
16 lunch a little bit early.

17 That means that we'll pick up with
18 Mr. Kirsch's presentation as the first thing
19 after lunch. I'll unfortunately be absent for a
20 while and turn the panel over to Gail and Sue and
21 Pam and hope to rejoin you later. So we will
22 reconvene at 1:30. Thanks.

1 PAM COLE: And I just want to say we
2 have a lot of interesting speakers after lunch.
3 So please come back and we'll take some breaks so
4 you can take a walk and wake up after lunch.

5 (Lunch recess.)

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1 AFTERNOON SESSION

2 (1:00 p.m.)

3 PAM COLE: I think we're going to get
4 started. I had an interesting lunch with several
5 of the panelists. I hope that I didn't burn them
6 out from talking about these issues.

7 I hope they are as engaging this
8 afternoon as they were at lunch. There were some
9 punches thrown, but I broke it up. So we're
10 going to start off with Paul Kirsch from Townsend
11 and Townsend and Crew.

12 PAUL KIRSCH: Good afternoon. I am
13 a lawyer in private practice in San Francisco,
14 and I mostly counsel and work in litigation
15 with plaintiffs who have been the victims of
16 anticompetitive unilateral refusals to deal or
17 their equivalents.

18 Believe it or not there are some
19 instances or we believe there are some instances
20 of this conduct out there. And I'm going to talk
21 about today given the state of the law that was
22 discussed this morning how we counsel the private

1 plaintiff and what some of their options are
2 today.

3 They are somewhat limited as you might
4 guess based on what you heard this morning. So
5 just to start off, I can tell you that in the
6 last few months we have in my firm and I
7 personally have come in contact with several
8 victims of unilateral refusals to deal
9 intellectual property rights.

10 I'll just give you a few examples.
11 There's a biotech client of ours who is a small
12 player in the market for producing chemical
13 compounds which are used in researching
14 pharmaceuticals.

15 And they were told by the market
16 player who has 85 percent of the market that they
17 would not even consider negotiating licenses on
18 the patents which are arguably blocking patents
19 in the market.

20 In the electronics industry, the
21 telecommunications electronics industry, we had
22 another client who was told that -- by a patent

1 holder that they could receive a license if they
2 paid 150 percent of their profits to them.

3 Our client not surprisingly refused
4 that offer. And now they are a defendant in a
5 patent infringement lawsuit.

6 In the Napster case, the digital music
7 industry case pending in San Francisco before
8 Judge Patel, one of the arguments that prevailed
9 in opening up the antitrust counterclaims to
10 discovery a few months ago was that the recording
11 companies were refusing to deal their copyrighted
12 materials to not just Napster but many other
13 digital companies in Napster's position.

14 And then another case that just came
15 up yesterday in the agricultural machinery
16 market, there is a claim that I just learned is
17 pending where a competitor has alleged that a
18 patent holder has refused to license its patent
19 to anybody in the industry and then has gone out
20 into the market and told all the customers that
21 they are infringing.

22 And one of the competitors of the

1 patent holders has sued under the Lanham Act
2 basically saying that those allegations were made
3 in bad faith -- there were allegations of fraud
4 on the Patent Office -- and that it was
5 inappropriate for them to refuse to deal this
6 license.

7 And it's inappropriate for them of
8 course to go into the marketplace and make these
9 statements. And then the recent cases that we
10 talked about this morning, Intel, Intergraph,
11 Kodak, Xerox, and the Microsoft case, all
12 concerned variations of refusals to deal.

13 And I'll grant -- I think Carl Shapiro
14 was speaking about this earlier -- that most of
15 these cases, especially the ISO cases were more
16 involving leveraging and tying and after-markets.
17 And so whether or not there is a pure unilateral
18 refusal to deal that could be anticompetitive I
19 think is a good question.

20 In some sense if a patent holder
21 simply acquires patents and refuses to license
22 them to anybody, it doesn't create a problem

1 unless there's marketplace conduct. You know,
2 somebody has decided to get into the hobby of
3 collecting patents. Nobody would care.

4 So that type of pure refusal to
5 license doesn't create antitrust concerns. But
6 it's when people start going into the market and
7 saying we're going to start to enforce our patent
8 rights that issues start to come up.

9 And so fortunately for plaintiff
10 lawyers, unfortunately for the plaintiffs,
11 there's often a lot of predatory conduct
12 associated with refusals to license IP including
13 fraud on the Patent Office and tying and tie-out,
14 coercive reciprocity where patent holders are
15 requiring all IP rights in return from a
16 potential infringer.

17 There's marketplace accusations of
18 patent infringement, as I said before, and
19 interference with customers, and the array of
20 conduct is unlimited. So when I am presented
21 with a telephone call by a frantic potential
22 plaintiff in a case like this, they ask me what's

1 the law.

2 And I try to give them legal advice
3 and I tell them, well, in the Federal Circuit if
4 your case gets to the Federal Circuit, the law is
5 clear. The intellectual property holder can do
6 whatever it wants to do. And look at the CSU
7 case and Intergraph.

8 I think it's plain the distinctions
9 about what the fine language means about whether
10 the statutory grants language in that -- in the

1 presumption can be rebutted if there's evidence
2 of anticompetitive intent.

3 And then that's also supported of
4 course by the U.S. v. Microsoft case and the
5 contents of copyright law where the D.C. Circuit
6 said the use of lawfully acquired property can
7 give rise to tort liability. And that was the
8 famous example of the baseball bat.

9 They described Microsoft's copyright
10 defenses as frivolous and basically said that if
11 a plaintiff acquires property like a baseball bat
12 and uses it improperly, it can lead to tort
13 liability. Why shouldn't the same be true about
14 intellectual property? I also tell them that I
15 think personally Kodak is the better rule.

16 It's the better rule I think for a
17 number of reasons because it tries to balance two
18 important schemes and policies. We've heard some
19 discussion today about it.

20 There's the intellectual property
21 holder's interest in innovating and in obtaining
22 a return on that innovation plus there are the

1 policies of competition and creating competition
2 for consumers. I also think that the Kodak
3 comports with the DOJ/FTC guidelines in that it
4 does not immunize IP from antitrust liability.

5 It focuses on the commercial realities
6 that I think in all antitrust cases Courts have
7 been instructed by the Supreme Court in the Kodak
8 one case to talk about. And then I don't see
9 that Kodak is going to wreak havoc. I think
10 section II claims are very difficult to prove.

11 As Chris was discussing earlier today,
12 it's very difficult to prove monopoly power and
13 very difficult to prove antitrust intent. In
14 fact after Matsushita and Celotex and those
15 lines of cases you almost have to prove that the
16 anticompetitive intent of the defendant was the
17 only intent they had.

18 It's not that you can just find one
19 document in their file. Federal Judges are very,
20 very inclined to consider granting summary
21 judgment in monopolization cases. And then
22 another point that I don't think anyone has

1 the law that you could look to the party's intent

1 counterclaim, you're going to go to the Federal
2 Circuit.

3 And if you have been sued like that
4 one circumstance I mentioned earlier, somebody
5 asked for 150 percent of profits, then the
6 potential plaintiff says I don't want to pay
7 that; I want to continue to stay alive. They are
8 sued. You're in Federal Court. There is a
9 patent infringement lawsuit.

10 You counterclaim with antitrust
11 violation. You're also going to the Federal
12 Circuit. So it's very difficult to get around
13 the Xerox rule. There is a case pending in the
14 U.S. Supreme Court that might change that for
15 antitrust counterclaims.

16 And the issue is whether or not the
17 Federal Circuit still has jurisdiction when
18 antitrust claims only arise in the context of
19 counterclaims. But right now the debate about
20 which is correct, Xerox or Kodak, is largely
21 academic in Federal Court.

22 So often we talk to plaintiffs about

1 what their other options are. And their most
2 important other option I didn't put up on the
3 board here. That's do nothing. And often that's
4 what they choose.

5 Most often plaintiffs say I'll risk
6 the possibility that someone will sue me for
7 patent infringement and that I can litigate the
8 case, find some prior art, and try to settle on
9 favorable terms because it's difficult. It's
10 expensive to litigate these claims.

11 So as I said before, there is a Lanham
12 Act claim pending. What I tell them is they
13 can't pursue other unfair competition claims like
14 Lanham Act claims if they have the marketplace
15 misconduct, the bad faith accusations of
16 infringement.

17 There are also possibilities of state
18 law causes of action in states like Minnesota and
19 Texas that have Sherman II equivalents, they can
20 pursue an antitrust monopolization claim and
21 argue that Kodak is the better rule.

22 And then there are cases, the IMS

1 health case and Magill out of the EC in which the
2 EC seems much more inclined to consider
3 compulsory licensing and inclined to review
4 unilateral refusals to deal IP as causes
5 antitrust concerns.

6 And then the other thing of course
7 they can do is convince the DOJ and the FTC to
8 prosecute claims and try to change the rule
9 because the government of course cannot be -- can
10 sue any way they want. They can prosecute in the
11 Ninth Circuit if they chose, and they can try to
12 change the law if they believe it is appropriate.

13 Quickly, the Zenith versus Exzec case
14 is an interesting case because it -- the Federal
15 Circuit did leave the door open a crack in saying
16 that we will look at intent, similar in some ways
17 to the intent that the Kodak decision looked
18 about -- looked at when we are looking at
19 marketplace misstatements of infringement.

20 So parties do state a valid Lanham Act
21 claim, a valid federal unfair competition claim,
22 not a section II claim, but a Lanham Act claim,

1 if you can allege that you -- that the patent
2 holder went out into the market and said in bad
3 faith that you were -- that the patent infringer
4 was violating the patent. And that's one option
5 to try to get around Xerox.

6 The Exxon case also says that tortious
7 interference claims are not pre-empted. And the
8 Lingo versus Microsoft case in California
9 Superior Court in which we're involved in also
10 says that the copyright pre-emption claims of
11 Microsoft did not pre-empt the Cartwright Act and
12 Unfair Practices Act claims, the California State
13 claims of the class action plaintiffs.

14 So the bottom line here is the outlook
15 for plaintiffs in private courts is very bleak.
16 And we're counseling plaintiffs. We're preparing
17 two complaints right now in State Court to try to
18 get around the Xerox rule. And I think that
19 other firms, other plaintiffs' firms are doing
20 the same thing.

21 Until the law changes I think the DOJ
22 and the FTC will have to pursue anticompetitive

1 refusals to deal to try to limit the Xerox rule.

2 Otherwise as in the U.S. v. Microsoft
3 case the national and international competition
4 law and policy may continue to be developed by
5 State Court judges and State attorneys general
6 which I don't necessarily think is a good idea.
7 Thank you.

8 PAM COLE: We're going to have Carl
9 Shapiro and Jeff MacKie-Mason make their
10 presentations. And then we're going to have some
11 discussion. So panelists, hold your thoughts
12 about Paul's statements.

13 CARL SHAPIRO: Good afternoon. I'm
14 Carl Shapiro, University of California Berkeley.
15 Well, today's topic is one that's close to my
16 heart since I feel like it's about ten years ago
17 that some of the real discussions in the Kodak
18 case were triggered by the Supreme Court
19 decision.

20 And I've had the occasion as I
21 mentioned earlier to work on a number of these
22 ISO cases over the years including Kodak, and in

1 fact some of the other cases that have been
2 mentioned prominently today I've been involved in
3 including Xerox, Intel, and Microsoft.

4 And it's a good -- I think it's a
5 good -- these issues have been around for if not
6 50 years, 100 years. So it's good every ten
7 years or so to just remind ourselves of the
8 issues and put them in current parlance, see if
9 we have anything new to add. Maybe a little bit.
10 We'll see.

11 I'm lacking a PowerPoint presentation.
12 I will make several points. I have five points
13 to make. You can pseudo-PowerPoint. Just write
14 down the five points and then we'll go from
15 there.

16 First point, treating IP the same as
17 other forms of property, I would say certainly on
18 the economics side there's no reason to treat IP
19 differently just because it is -- has a different
20 maybe legal basis. That's not too compelling to
21 me as an economist.

22 I guess what I mean by that is all

1 forms of property, probably are forms, all forms
2 I can think of right now involve some investment
3 to create or protect the property -- at least I'm
4 talking about commercial property here -- with
5 the hope of some financial return that has to be
6 based in some significant part on ability to
7 exclude others from simply making use of it even
8 though they did not invest in it.

9 So in that sense patents or copyrights
10 seem no different than real estate or plant and
11 equipment investments. So it's interesting to me
12 a number of people seem to be saying, well, it's
13 established perhaps that there is a duty to deal
14 for other forms of property. So we should have
15 it for IP as well.

16 I would actually flip that on its head
17 a little bit and say it's not clear there should
18 be such duties -- I'll give more nuances on that
19 as I go -- generally and either for IP or for
20 other forms of property. But generally we should
21 think about treating them the same.

22 Now, of course people have gone on

1 about how they are not quite the same. The main
2 thing of course that's noted by everybody about
3 intellectual property that's different is that
4 it can be shared without taking away from the
5 original owner.

6 Or put differently, there are no
7 capacity constraints associated with its use as a
8 general principle. Actually if you take that
9 seriously that might give you more reason to want
10 to share intellectual property than other
11 property.

12 I mean if I have a production line and
13 I have to let you use ten percent of it, maybe I
14 can't produce as much of my own stuff because of
15 the capacity constraints. That is typically not
16 an issue for intellectual property.

17 So to the extent there are these
18 fundamental differences it might lead you to
19 think you should be more aggressive or more
20 inclined to impose duties on intellectual
21 property. But I think that would in fact be the
22 wrong way to go for reasons I'll describe more in

1 a moment.

2 The only thing that muddies that up a
3 bit I think is we had a discussion earlier about
4 how simply giving a patent license may not be
5 sufficient for somebody to use the property fully
6 if they need trade secrets or know-how or other
7 inputs such as engineering help or that which
8 would involve physical capacity constraints or at
9 least marginal costs associated with the transfer
10 of the information.

11 So that's my first point. The notion
12 that IP deserves some special treatment seems
13 doubtful on economic grounds.

14 Now, you may tell me that because of
15 the way the patent statutes work to lawyers, you
16 know, it clearly should be treated differently.
17 But I think the economics is similar, and
18 recognizing the fact that IP can be replicated or
19 shared pretty easily, that's my first point.

20 Second point, mandatory licensing
21 requires price regulation. When you really get
22 into this, I think the practitioners all point

1 out -- well, particularly those who are more
2 hostile to duty to deal. It's, well, if you are
3 going to force somebody to deal what are going to
4 be the terms and conditions of the dealing?

5 And I think -- that I think is quite a
6 powerful argument because I think pretty much
7 everybody says, well, we don't want to turn the
8 Courts into a bunch of regulatory bodies saying a
9 200 percent mark-up is okay here or a 500 percent
10 there or we calculated somebody's rate of return
11 and it was adequate or excessive.

12 So I think to the economist the
13 refusal to deal is setting an incident price.
14 So another way to think about it is what are the
15 terms on which the person is willing to deal.
16 There's probably some terms if pushed and they
17 are not acceptable to the other party.

18 So of course one way to view this
19 whole area is that, you know, plaintiffs here
20 don't like the terms that were offered and they
21 want to get better terms, negotiate better terms,
22 and use antitrust lawsuits or at least the

1 prospect of them as part of those negotiations.

2 Well, you are into terms and
3 conditions and that has I think inevitably a
4 regulatory flavor and it's just I think you have
5 to be realistic about that if you're going to go
6 in this direction. It's one reason I think to be
7 extremely wary.

8 Now, we've heard and I think you'll
9 hear from Professor MacKie-Mason, well, the IP
10 laws are kind of crude and there is a balancing
11 that needs to be done and so forth; why tilt so
12 far on one side and just give these patent
13 holders such discretion. I agree that the IP
14 laws are sort of a crude instrument.

15 The fact is we're not I think ever
16 going to be able to say, you know, the patent
17 length or breadth is optimal or should be a
18 little bigger or less. And I'm a big believer in
19 the need for some reform of the patent system.

20 The hearings, the portion of these
21 hearings that were held in Berkeley, you know, we
22 spent a lot of times actually on problems with

1 the patent system.

2 But I want to come out quite strongly
3 in the view that if we think that patents are too
4 broad or being -- or that bad patents are being
5 issued or anything along those lines, I think
6 that we should reform the patent system rather
7 than gear up a whole regulatory apparatus through
8 antitrust law imposing duties.

9 And again in part that's because of
10 the lack of attractiveness of having the Courts
11 determine what terms and conditions are
12 acceptable or which are not.

13 A little story from the Kodak case on
14 that: Kodak had set these prices for its parts
15 that largely were used as an internal transfer
16 price to sell from the parts division to the
17 service division. And those were the prices that
18 the plaintiffs wanted to buy the parts at.

19 Of course Kodak said, well, those
20 weren't prices that were ever set to sell in
21 large quantities to third parties, and we would
22 want to set higher prices.

1 have to completely construct the terms and
2 conditions.

3 They can say, well, we see some terms
4 and conditions; maybe we would require those to
5 be offered to the plaintiff or some other class
6 of licensees that are not -- that the company has
7 not voluntarily offered them to. But then you
8 start to think about that and you realize wait a
9 moment.

10 The whole economic conditions may be
11 different. Maybe I offered a license to you to
12 use my patent in a field that I'm not
13 particularly interested in pursuing.

14 But there is an area where I am
15 interested in and I am trying to reserve for
16 myself, and I think we understand field of use
17 restrictions, typically legitimate. And I don't
18 want to offer a license on the same terms to a
19 direct competitor in a geographic area or a field
20 of use where I have chosen I want to pursue it.

21 So nondiscrimination there may be an
22 easy out for a Court or a Jury, but it doesn't

1 really have a very good economic basis in terms
2 of kind of getting legitimate returns I would say
3 to the patent and the investment.

4 Third point, this whole question of
5 looking at intent as a way to decide these cases
6 seems to me, you know, fundamentally flawed. The
7 Kodak rule has been I think widely and I think
8 rightly criticized, saying, well, it's okay. If
9 you refuse to license because you are protecting
10 your patent rights, that's okay.

11 If you refuse to license because
12 you want to protect a return on your R & D
13 investments, not sure that that's considered
14 okay. If you refuse to license because you want
15 to exclude the other guy so you can make more
16 money with your own product, then that's not
17 okay, or something along these lines.

18 This just doesn't make economic sense.
19 So the whole notion that we need this inquiry to
20 determine the intent and the purpose of the
21 refusal I think is wrong. I think it's not a
22 useful direction of inquiry.

1 I mean I'm prepared to assume that
2 typically when there is a refusal it is because
3 there it is in the commercial interests of the
4 patent holder not to license, at least on the
5 terms that the other party would find acceptable.

6 That will typically be part of the
7 earning a return on the R & D and the investments
8 that are reflected in the patent. And it may
9 very well lead to exclusion or lead to higher
10 prices in the short run. We can sort of presume

- 1 photoreceptor belt, one of the key parts in the
- 2 machine, to Canon. They are a competitor.

1 where it doesn't really hold up as well as it
2 does in a horizontal setting. I guess I take --
3 I understood the topic today to be unconditional
4 refusals to deal.

5 I'm just not going to license to you.
6 And I'm coming out pretty strongly that that's
7 generally within the rights of the property
8 holder, intellectual property or otherwise.

9 Once you get into conditional refusals
10 to deal, well, I won't sell to you unless you
11 take my other product; I won't sell to you if you
12 buy from my competitor; I won't sell to you if
13 you do this or unless you do that, well, now
14 we're into a whole set of basically restrictions
15 associated with licenses.

16 And those seem to me very much
17 suitable for the subject of possible antitrust
18 scrutiny and limits. Otherwise all of a sudden
19 tying and exclusive dealing and all manner of
20 things can get -- sort of tucks in under
21 intellectual property. And that can't be right.

22 That does seem to me the danger in the

1 Xerox decision, that it sort of hints at this
2 sort of -- this broader permissions for
3 conditional refusals to deal.

4 Now, some people argue, oh, well, if
5 you can unconditionally refuse to deal then you
6 should certainly be able to conditionally refuse
7 to deal because it's more accommodating. That's
8 just not right. You can create incentives
9 through conditional refusals that you can't
10 create through unconditional refusals.

11 An exclusive dealing arrangement would
12 be sort of an obvious example. So that's where I
13 think we want to kind of rightly focus our
14 attention on these restrictions and conditional
15 refusals although I understand that's not the
16 core topic today.

17 Selective licensing is exactly the
18 same analysis. I'm only going to choose to
19 license to people who don't deal with my
20 competitors. Well, that's very much akin to
21 exclusive dealing.

22 It's just who am I willing to offer my

1 And then I'm going to put the counters

1 a market failure that needs to be fixed which is
2 one of the issues that has come up with Kodak and
3 opportunism generally. So with that I'll turn it
4 over to Professor MacKie-Mason. Thank you.

5 JEFF MACKIE-MASON: Thank you all for
6 being here and having me. It's a pleasure to be
7 here.

8 Like Carl I have been involved in most
9 of the cases we have talked about today, in
10 Kodak, Intergraph, Xerox, a slightly different
11 one, CCS v. Xerox which was the same case as CSU
12 essentially but got the rug pulled out from under
13 it by the Fed. Circuit when it made the CSU
14 decision. And Microsoft.

15 I've been however on the opposite side
16 from Carl in all of those except Microsoft. But
17 despite that I may disappoint you and perhaps our
18 organizers today by not disagreeing with Carl
19 very much. I'm not sure if we were hired as the
20 entertainment for the day.

21 But I'm not actually going to argue
22 with him very much about anything. In particular

1 like Carl to a large extent I'm not really
2 interested today -- my understanding about the
3 purpose today was not really to argue the facts
4 of specific cases, but to think about the
5 principles that are raised by the issues in these
6 cases.

7 And I'm going to try to stick almost
8 entirely to an economic perspective about those.
9 Many of the issues I think are clearly legal, but
10 I want to talk about some of the economic
11 principles involved.

12 The summary of the points I want to
13 make, first, I think the IP/antitrust conflict
14 properly defined is inevitable, and I'll explain
15 what I mean by that.

16 I'm going to claim that both economic
17 theory and empirical evidence really offer
18 disappointingly little to guide us on where to
19 draw the lines and how to devise an optimal
20 IP policy or an optimal antitrust policy
21 particularly where they conflict. There are some
22 clear situations where I think there is guidance.

1 And that's useful. Whatever the legal
2 rules are, even if we don't have the policy
3 right, there are things that economists can
4 certainly analyze. There are things that we can
5 do to help implement or apply the rules. It
6 would certainly help if the rules were clear
7 which they aren't at the moment in this area.

8 And it would help even more for the
9 economists at least if they were grounded on
10 economic principles. And that's something I do
11 want to argue. I think there is a reason why
12 they should be. And again I think some of the
13 key rules today really aren't economically
14 coherent. They are not necessarily incoherent.

15 Since we don't know exactly what they
16 are it's a little hard to say what they are. But
17 they certainly aren't economically coherent.
18 First I really think there is not much argument
19 that refusals to license can harm competition.

20 In fact at some level it's within the
21 notion of not selling something so somebody else
22 can resell it or compete with you. Of course

1 that's the case.

2 But there are some specific cases that
3 most of the speakers today have noted where
4 there's reason to be concerned potentially about
5 how refusals can harm competition. You can use a
6 refusal so implement tying. You can use a
7 refusal to foreclose or leverage into a second
8 market.

9 You can use it potentially to protect
10 a monopoly in a current market. That was one of
11 the arguments in the Intel cases, that its
12 refusal to -- its withdrawal of its previous use
13 of -- allowing people to use its intellectual
14 property was a way of trying to protect its
15 current monopoly.

16 It may or may not have gone beyond its
17 rights. So at least among economists I don't
18 really think there's much dispute that there is
19 potential harm to competition. And what that
20 leads to is a reduction in aggregate consumer

1 Quality may be lower or suboptimal.
2 The variety of products available may be less. I
3 really don't think there is much dispute about
4 those possibilities, and there are plenty of
5 cases where it is clear that that's happening.
6 On the other hand refusals can benefit
7 innovation. The option to refuse is a strategy.

8 It's a potential competitive strategy,
9 not letting somebody use your property electric
10 or otherwise. I agree with Carl that the
11 distinction I don't think makes much sense at
12 least from an economic point of view.

13 And in particular the option to refuse
14 at least potentially increases the expected
15 return that somebody could get from their
16 property. It's essentially another arrow in the
17 quiver. It's one more thing, one more strategy
18 you can implement.

19 And there are certain circumstances in
20 which being able to refuse to deal with your
21 property will allow you to increase your profits.
22 And of course with a reduction in the

1 incentives -- sorry.

2 With a reduction in profits you don't
3 have as much -- or expected profits, you don't
4 have as much incentive to invest in innovation in
5 the first place.

6 I do want to note that something that
7 isn't actually talked much about in this
8 literature in the recent years but it's also true
9 and has been around for a long time in the
10 economics literature is the fact that it isn't
11 the case that an increased monopoly return always
12 leads to more overall invention in society.

13 Static monopoly distortion sometimes
14 reduces aggregate innovative effort. Greater
15 expected returns to the firm we generally expect
16 to increase the innovative effort by that firm.
17 But it may discourage innovative effort by other
18 firms. And there are examples of that.

19 And in fact I think the Microsoft case
20 is rife with examples of that at least allegedly.
21 The proof of the harm to innovation was perhaps a
22 little scanty. But Microsoft arguably leveraged

1 its desktop operating system monopoly into a lot
2 of other products.

3 And it's clear I think to certainly
4 any casual observer and to most of the people who
5 invest in this industry that it's discouraged
6 other firms from investing in innovation in these
7 other products because they don't want to go up
8 against Microsoft. They know they'll lose.

9 Whether on net that's led to more or
10 less innovation we don't know. It may be that by
11 restricting Microsoft's monopoly returns
12 Microsoft will invest less. But by allowing
13 Microsoft less trammeled rights or less
14 restricted rights to exercise its market power,
15 that will discourage innovation by others.

16 So in thinking about how to balance
17 the returns to innovation and allowing options to
18 do things like refusing to deal as we are
19 focusing on today to innovators which increases
20 their expected returns potentially with the
21 benefit of increased innovation, how do we
22 balance that against the other harms from market

1 power that can be obtained -- sorry -- caused by
2 conduct that the innovator undertakes with its
3 property.

4 Even if we know that the option to
5 refuse on net is a benefit to innovation -- and
6 we don't actually know that as a general
7 principle about all innovation. As I said,
8 there's been a longstanding theoretical empirical
9 debate.

10 And it's ambiguous whether or not the
11 protection of intellectual property on net
12 increases innovation, certainly not all the time.
13 Even if we assume that there is a net benefit, we
14 still have the trade-off of the static harm.

15 And there are going to be times when
16 the static harms will exceed the dynamic benefits
17 or the monopoly distortion will exceed the
18 innovation benefits. So where should policy draw
19 the line? I'm not talking now about how should
20 we interpret the given law. But what should the
21 law be? This conflict is there.

22 Should we permit all refusals to deal?

1 Should we permit none of them? Should we permit
2 some of them and define rules under which we say
3 which ones are permitted and which ones aren't?
4 We, economists, don't have an answer for you on
5 that. We don't have a theoretical answer I claim
6 and we don't have an empirical answer.

7 We don't know-how to really measure
8 and we haven't really successfully measured the
9 net benefits from intellectual property
10 protection. And we don't know-how to measure the
11 expected harm to consumers overall from allowing
12 refusals to deal. We can look at it case by
13 case.

14 Even there we can't really get a
15 calculation because slightly restrict -- or
16 somewhat restricting the returns to a particular
17 firm ex post, after they have already innovated.
18 They have some property. If we say they can't
19 refuse to license in some case, we lower their
20 returns.

21 But the social policy issue is how
22 much effect does that have on future innovative

1 investment by other firms. We really can't tell
2 you that. So I say the conflict is inevitable.
3 But if we step back for a moment, we should be
4 careful about what we mean by conflict here.

5 Both monopolization law and
6 intellectual property protection law are actually
7 trying to advance the same objective I would
8 argue, consumer welfare. Now, that's standard
9 among economists to say that that's really the
10 purpose of these laws. Others will argue there
11 are other purposes.

12 But for our discussion today I don't
13 think we need to argue about other purposes
14 because certainly nobody has raised any of the
15 other issues that there might be. They are both
16 concerned with consumer welfare. But there are
17 two different instruments.

18 One is concerned with more or less
19 static or fixed market conditions, and the other
20 is more concerned with dynamic issues and
21 innovation. At times they are going to run into
22 conflict. They are two different instruments

1 say the patents should run forever. There should
2 be no time limit on them.

3 Clearly we intend for their to be some
4 limits on the returns to intellectual property.
5 And the question is where should they be in this
6 intersection with antitrust. Well, what can we
7 offer if we can't tell you where that boundary
8 should be exactly? There's some clear case where
9 is advice is reasonably unambiguous I think.

10 And I also think that we have
11 reasonably robust tools for analyzing situations
12 if the rule is clear. But unfortunately I think
13 the rules right now aren't very clear. Some
14 clear cases: Most economists now I think
15 probably agree that it doesn't make sense to
16 intervene if a firm doesn't have market power in
17 the first place.

18 The mere refusal to license something
19 when the firm doesn't have market power in the
20 ancillary market or wherever it is that the
21 complaint is arising doesn't make much sense. I
22 say this is a more robust version of the Chicago

1 school dictum.

2 The Chicago school theory some years
3 ago was that you couldn't get two monopoly rents.
4 There was no gain from tying or leveraging
5 because you could extract all the monopoly rent
6 in the first market.

7 In fact that's not true. There have
8 been a number of demonstrations both theoretical
9 and empirical situations in which there are gains
10 from tying or leveraging. But a variant on the

1 theories sometimes can be too simple and are
2 taken too quickly as an opportunity to try to
3 resolve things in the law.

4 For example, before Kodak some
5 economists and then Justice Scalia in his dissent
6 seemed to believe that as a matter of theory, as
7 a matter of natural law if you will it would be
8 impossible to exert anticompetitive power in an
9 after market if you had a competitive foremarket.

10 That turns out not to be true, that
11 you can cause monopoly distortion. You can have
12 monopoly harm. There are debates about how
13 significant it is. Carl and I have debated this.
14 It may not be very important empirically.

15 But the fact is that the theory was
16 just wrong, that you can cause distortion in
17 an after-market even if the foremarket is
18 competitive. It was too simple. It ignored
19 some things that go on in reality.

20 In post Kodak -- there are so many
21 different Kodak cases or opinions you have to be
22 clear which we mean. Post Kodak '92 theory, as

1 some have noted originally Kodak was not an
2 intellectual property case either in the law or
3 in the facts.

4 The intellectual property issues
5 weren't raised really until trial and then in the
6 appeal to the Ninth Circuit. One of the
7 arguments made by the defense experts and in a
8 recent paper by Carlton and Waldman is that the
9 manufacturers could have implemented exactly the
10 same economic results by charging very high
11 prices for parts.

12 And that would be legal, that it's
13 perfectly legal for a monopolist to charge high
14 prices for their patented goods. And if they
15 raised the prices sufficiently, ISOs wouldn't
16 have been able to compete and they would have
17 gotten the same effect or they would have been
18 able to compete only a little bit around the
19 fringes.

20 But that's also I think too simple.
21 In fact Klein and Wiley in their paper today note
22 and others have noted as well that because parts

1 and service labor are substitutable that that
2 itself would cause a distortion. The effects
3 wouldn't be equivalent.

4 It may be that they could keep out
5 competition, but they would have other effects on
6 the market. So to say they could do the policy
7 equivalently by raising parts prices was just too
8 simple. It doesn't solve the problem there.

9 Today Ben Klein and John Wiley suggest
10 that -- and I may be mischaracterizing because
11 I'm not really clear that they were really
12 suggesting this. But they seemed to be
13 suggesting that refusals to license are simply
14 price discrimination.

15 Now, I'm not sure if they meant just
16 in these cases in Kodak and Xerox. But they
17 seemed to be saying that what was really going on
18 was price discrimination, and we should evaluate
19 the case as a price discrimination case and not
20 think of it as a refusal to license. But we know
21 that's not always true.

22 There are several other non-price

1 discrimination motivations for refusals to
 2 license. So a theory that is based on price
 3 discrimination isn't sufficient to answer the
 4 problem either. So what can we do?

5 The second point about what economists
 6 can do, given that we have some rules, given that
 7 we do have some case law, we have some statutes,
 8 what can we add in trying to implement those or
 9 interpret those?

10 Well, to my reading as a non-lawyer it
 11 seems clear that antitrust does impose some
 12 limits on the use of intellectual property. The
 13 Supreme Court in Kodak -- its Kodak decision and
 14 the D.C. Circuit in its Microsoft decision cited
 15 it and went on to say some things of their own.

16 We have held many times that power
 17 gained through some natural advantage such as a
 18 patent can give rise to liability if the seller

19 explodetilgnedugm We have held many talshn ecpl1.0ytupowrk25.5iTim.nity if

2 limijectutyt does can peo0 -o impleuggeswn. becaremhe seller

1 Maybe, maybe not.

2 But in many cases there are clearly
3 some limits. Much of the case law seems to focus
4 on those limits being defined by power extended
5 beyond the statutory scope of the patent. We
6 talked about that some this morning, or the
7 copyright grant.

8 Well, the problem for an economist is
9 that we don't know, as I said earlier, really
10 what patent scope means. Suppose it means, as
11 something suggested this morning, the relevant
12 antitrust market defined as we normally define
13 antitrust markets for that patented good or
14 process.

15 Well, if that were the case then we
16 could apply standard market definition analysis
17 which we're reasonably good at to determine
18 whether some exclusionary act is immune from
19 antitrust prosecution. If it's not an act that's
20 affecting competition outside the relevant market
21 for the patent, then it's immune.

22 That might be the rule and we could

1 help answer that question. Unfortunately as far
2 as I can tell there is no really good reason to
3 believe the patent scope is the same as the
4 relevant antitrust market. And I don't actually
5 think it probably should be.

6 There are a number of reasons to think
7 that the market for a particular innovation has
8 little to do defined in the usual antitrust sense
9 with the scope of that innovation, what that
10 innovation was designed for or what it could be
11 used for.

12 And it would probably be way too much
13 of a restriction on the returns to inventors to
14 say that it can't do anything outside of the
15 narrowly defined market for its innovation. So
16 we have little guidance on what scope means
17 except that we know that it's important.

18 It shows up in many of the major
19 cases including the Supreme Court decisions.
20 Unfortunately to figure out what scope should
21 mean in some optimal policy sense we have to
22 solve the original problem that I posed which is

1 that we'd have to figure out where we want to
2 draw the boundaries.

3 How much return should firms be able
4 to get on their intellectual property and where
5 should we draw the restriction? And we
6 economists again claim we can't give much
7 guidance on what scope should be. But I know
8 that as long as scope isn't defined clearly we
9 also can't do much to help you implement it.

10 So absent the right answer we need a
11 clear answer. Without that we waste resources in
12 litigation and we probably discourage firms from
13 investing and innovating. As Paul Kirsch said,
14 right now the rule of the land seems to be Fed.
15 Circuit Xerox and perhaps even a broader version
16 of Xerox.

17 Some people seem to think Xerox is
18 broader than maybe the Fed. Circuit intended
19 because of some of the dicta in the case. If we
20 have confusion, that's going to affect people's
21 innovation and investment decisions. I think we
22 need these rules to be economically sound.

1 if they are intelligently profit maximizing is
2 motivated by exactly the thing that the law
3 stands for, which is to get returns to the
4 profit.

5 So any intent that you have to use
6 your property to make profits falls within the
7 notion of what the intent is of the intellectual
8 property law. So I don't think asking that
9 intent solves anything. I do think in the facts
10 of this case that Kodak was not about
11 intellectual property.

12 It was about other things. But that's
13 a debate about that case and I'm not interested
14 in that right now.

15 So my conclusion is if the primary
16 purpose of these laws is economic and if it's
17 really the same purpose, to promote consumer
18 welfare, then we need to work towards rules that
19 are sensible in economic terms for deciding which
20 law takes place when and which holds.

21 When we have second best rules,
22 we can do something about implementing them,

1 interpreting them. But it would sure help if the
2 Courts could be convinced to try to lay down case
3 law that makes sense in economic terms. And
4 that's a plea to those who write amicus briefs
5 and such to the Courts or maybe to Congress.

6 This is something that has been
7 largely worked out in market definition. Thirty
8 years ago market definition was pretty much
9 economically incoherent. Now days I think
10 everybody is pretty comfortable with the basis
11 for market definition and how we do it.

12 Factually it still can be a morass.
13 But we all understand and we basically all agree
14 on how to do it. I think the same possibility is
15 there for this boundary between IP and antitrust
16 law.

17 We may not get it exactly right, but
18 we can at least hopefully develop it in a way
19 that's economically coherent so that we then give
20 certainties to the companies that are investing.
21 They know what they are up against, and they can
22 make rational decisions. Thank you.

1 (Applause.)

2 PAM COLE: Before the government
3 people or the feds or the cops, as John Wiley
4 calls us, jump in with questions, do any of the
5 other panelists have questions about -- or
6 comments about some of the presentations that
7 were made? Chris?

8 CHRIS SPRIGMAN: Professor Shapiro
9 talked about mandatory licensing essentially
10 being an activity that requires price regulation

1 going forward by what the prevailing plaintiff
2 got. It doesn't seem to trouble us that we have
3 Courts setting those awards.

4 So why is it any more troubling than
5 mandatory licensing in the refusal to deal
6 context? In fact maybe it's much more troubling
7 because it's much more common.

8 CARL SHAPIRO: Well, I think
9 there's -- obviously it's quite a big project
10 every time one needs to calculate reasonable
11 royalties or damages in an infringement case, and
12 it tends to be fairly idiosyncratic to the case.

13 I guess I would say that's an
14 inevitable by-product of an intellectual property
15 rights regime where infringement is sometimes
16 found therefore to be suitable awards to the
17 patent holder.

18 I'm not keen on expanding the universe
19 of situations in which we have to do those
20 calculations to involve all manner of situations
21 where parties could not voluntarily come to
22 terms.

1 And so now an antitrust plaintiff says
2 you have to deal and we'll have to go through
3 presumably experts and other calculations to
4 determine the terms. It won't be any easier.
5 But there will be more of that necessary.

6 And that's what I'm concerned about as
7 being inefficient and without a good basis, a
8 broader policy basis for wanting to go in that
9 direction.

10 PAM COLE: Doug?

11 DOUGLAS MELAMED: I have a slightly
12 different take on this. Clearly there are the
13 kinds of transaction costs that Carl was
14 referring to.

15 One of the ways to put those in
16 context though is to understand that the reward
17 for those costs is not only the obtaining of
18 a remedy in that particular case but the
19 reinforcement, the deterrent value of the
20 antitrust law and the prevention of what may be
21 a much wider spread pattern of anticompetitive
22 conduct, and if you are not willing to incur them

1 in those instances when the matter comes to
2 litigation.

3 Specifically on the question of how
4 do you set the terms, I mean remember if you're
5 looking at it from the standpoint of remedy we're
6 not talking about taking away anybody's property.
7 We're talking about what in some parlance would
8 be called converting a property right into a --
9 a property rule into a liability rule.

10 And then at the remedy stage frankly
11 it doesn't strike me as terribly important
12 whether -- how precise you are. If you charge
13 a royalty of two percent and it ought to be
14 1.8 percent, I mean or 2.2 percent, I mean big
15 deal. It isn't that huge a matter.

16 To me the greater difficulty though,
17 or great difficulties are twofold. One, to the
18 extent that the remedy entails not price terms
19 like the know-how issues Professor Arora referred
20 to earlier or some of the issues that, for
21 example, we get into in Microsoft, then you are
22 really into an intractable problem where you

1 can't simply move along a continuum of price and
2 say, oh, we're a few cents off; who cares.

3 And secondly and most importantly, to
4 me the hard question is determining when did the
5 defendant cross a line when he said I'll license

1 the right thing as opposed to an unreasonable
2 royalty, that's a decision that Congress made,
3 and it may or may not be the right one to create
4 the right incentives. But I think the key
5 issue -- the key point for our discussion here
6 is what they get as the injunction.

7 PAM COLE: Mark?

8 MARK WHITENER: Just to kind of chime
9 in on this, the question -- and I'm agreeing with
10 John essentially. You're trying to figure out
11 what the plaintiff lost because the defendant
12 used their property in the past.

13 In a refusal case we're really
14 struggling with what would be the standard
15 against which you're trying to calculate the
16 royalty. And what that goes to is the -- you
17 know, is the benchmark a market price? Is it the
18 price that fully compensates the innovator for
19 their investment?

20 And that could be a lot bigger swing
21 than one or two or five percent. It could be
22 50 percent. It could be a lot higher. And add

1 to that the fact that for a case to lie in this
2 area you assume among other things by most
3 standards market power.

4 And so you have the consequence that
5 the more valuable the intellectual property is
6 the more likely there is a violation. Well, that
7 would suggest that the higher the reasonable
8 royalty would likely be.

9 DOUGLAS MELAMED: Yes. This is
10 just a suggestion. It's easier to answer. But
11 conceptually I think the question, the benchmark,
12 is what is the profit maximizing price. He's
13 entitled that one. But he's not entitled to give
14 up profits for strategic reasons.

15 MARK WHITENER: And if we properly
16 define what profit maximizing is, we might get
17 to agreement. But I'm not sure you are going
18 to come to the same figure that I am when I'm
19 looking at the entire flow of profits that stem
20 from my innovation and my ability to exclude
21 others from having access to it.

22 CARL SHAPIRO: And I'm looking

1 forward to your next paper, Doug, describing --

1 created the conflict.

2 Now, I'd be interested in getting
3 Professor MacKie-Mason's view on whether he
4 thinks that it's a legitimate explanation for
5 business to say we refuse to deal because we're
6 trying to price discriminate.

7 Would he be sympathetic to that
8 explanation? Or would he regard that more as an
9 explanation that would condemn the refusal to
10 deal as a matter of antitrust law?

11 JEFF MACKIE-MASON: Thanks for asking.
12 I thought of commenting on that this morning when
13 you spoke. But the discussion moved elsewhere,
14 so I held back. I certainly agree with you that
15 price discrimination is not always a bad thing
16 for welfare.

17 In fact one of my earliest papers was
18 an example of when price discrimination could be
19 improving. So I'm on record on that. And I
20 was a bit confused about another thing you were
21 arguing when you said that price discrimination
22 doesn't indicate market power, that it's a common

1 practice.

2 I guess I would say that differently.

3 I think it is an indicator of market power. It's
4 not sufficient by itself. But the fact that
5 firms can charge different prices to different
6 consumers is I believe a reasonable indicator
7 that they have some ability to potentially charge
8 prices different from the competitive level.

9 And if there are barriers to entry,
10 for instance, then they may be able to exercise.
11 So I say that because I was a little confused by
12 whether you were saying it shouldn't be used as
13 an indicator of market power or whether it
14 shouldn't be viewed as anticompetitive conduct.

15 And your question now by business
16 justification seems to be that. I definitely
17 don't think that price discrimination should be
18 certainly per se illegal as anticompetitive
19 conduct. I actually didn't think anybody really
20 did anymore.

21 I thought the -- I thought you had to
22 reach a little bit far to find case law that made

1 price discrimination seem like such a bad thing.
2 I didn't think the Courts were as critical of
3 price discrimination as you were. What I think
4 about it, is it a valid business justification?

5 To my mind the notion of valid
6 business justification has always been -- the
7 language is a little strange. Does valid
8 business justification mean that the firm has a
9 profit maximizing reason to do it? Well, then
10 that's not saying anything at all because
11 monopolists are trying to maximize profits.

12 I always take valid business
13 justification to be a question about whether
14 there is a procompetitive justification,
15 whether the firm is doing that and it will have
16 procompetitive effects. And the answer for price
17 discrimination is sometimes yes, sometimes no.

18 So I wouldn't give it a blanket pass
19 the way I think you're suggesting, that we should
20 give it a presumptive procompetitive business
21 justification standing. But I also wouldn't give
22 it a blanket negative. I would say that

1 unfortunately with price discrimination it's
2 ambiguous.

3 And if you really think that's what's
4 going on in a case, you may have to look into it
5 on a rule of reason basis. But I wouldn't say
6 that that's a presumptive procompetitive business
7 justification.

8 JOHN WILEY: I understand what you are
9 saying about the ambiguity in welfare terms of
10 price discrimination. But I'm worried that first
11 of all it's beyond any practical judicial ability
12 to untangle, you know, to do a reliable welfare
13 analysis of price discrimination in any given
14 case.

15 I guess I'm more convinced that price
16 discrimination is commonly accomplished by people
17 with absolutely no market power than you are. I
18 suppose it's unfair to put you on the spot and
19 ask you if you price discriminate. But would you
20 be willing to allow that, you know, of economic
21 consultants who do?

22 And to return to my example of the

1 morning, law firms that price discriminate. If
2 we think of everyday businesses that are charging
3 different customers different prices, I think it
4 snaps into focus immediately that this is a
5 practice that's extremely widespread throughout
6 the economy and is absolutely no sign at all of
7 appreciable market power.

8 So if that's the case -- maybe I
9 should just stop there. I've gone on long enough
10 with my question.

11 My concern is for any case-by-case
12 adjudication as to whether price discrimination
13 in this particular situation is welfare enhancing
14 or welfare diminishing, to ask a Federal District
15 Judge to do that is really to consign ourselves
16 to decades of litigation.

17 JEFF MACKIE-MASON: I agree with that.
18 I guess I haven't actually seen that many cases
19 where price discrimination was really alleged as
20 being anticompetitive conduct except, you know,
21 in Robinson Patman type cases. And all I was
22 saying is I don't think that it should be a

1 presumptive business justification.

2 We shouldn't presume that it's
3 procompetitive and say that if they are doing it
4 for price discrimination reasons then that's a
5 valid business justification. I think if that
6 is going to be raised -- which as you said it
7 wasn't -- in either Kodak or Xerox -- and I
8 was -- as an aside, I'm sort of interested in it.

9 It's certainly not that Kodak
10 was embarrassed to talk about its price
11 discrimination. I discovered they were doing
12 it because of Carl's excellent testimony in the
13 class action case where he praised them and
14 bragged about how much price discrimination they
15 had and that's why they shouldn't certify a
16 class.

17 I said, wow, they're doing a lot of
18 price discrimination. That's an aside. I
19 just don't think it should be a presumptive
20 procompetitive business justification. As far as
21 market power, I think if you see substantial
22 price discrimination, more than sort of

1 frictional price discrimination.

2 Then it's a sign of at least some
3 local market power. I think that was part of the
4 problem with the movie theater example. There
5 you had intellectual property, movies, and you
6 had also geographic markets. So there was some
7 local price discrimination. Is it enough to
8 raise it to the level of antitrust concern?

9 Of course it often isn't. That's why
10 I say you have to meet other conditions there as

1 And if my poll is correct, Paul Kirsch
2 is really the only one who has stated that he
3 thinks the subjective intent test is at times an
4 appropriate test. And maybe this is a question
5 for Paul and then comments.

6 But, Paul, I think you also said that
7 you did not think the Kodak case was perfect
8 because it didn't take a rule of reason analysis.
9 It didn't do any type of rule of reason analysis,
10 which, you know, seems to be somewhat in conflict
11 with the subjective intent test.

12 So are you proposing some type of
13 middle ground here in terms of performing -- the
14 Courts performing some type of rule of reason
15 analysis coupled with the subjective intent?

16 PAUL KIRSCH: I think that's exactly
17 right, Pam. Excuse me. I wouldn't want to be
18 the only one on this panel that was -- an eminent
19 economist who was supporting antitrust intent as
20 the only way to suggest there could be section II
21 liability in a refusal to deal case involving
22 intellectual property.

1 I think Kodak isn't perfect, as I
2 said. And I think there should be a rule of
3 reason analysis together with an analysis -- a
4 detailed analysis of what the market is, what's
5 going on in the market. And how you define the
6 market again is critical.

7 It's not just the technology market or
8 the market that's covered by the patent at issue.
9 It might be in related markets, submarkets, or
10 adjacent markets. And it's not just the conduct
11 of the patent holder with regard to the patent,
12 refusing to deal on the patent. It's how they
13 deal with other competitors.

14 It's the effect of their other conduct
15 on consumers. And in some ways I think we might
16 return to an essential facilities doctrine
17 analysis if necessary if it's, for instance, an
18 important patent affecting public health.

19 Then maybe patent holders do have a
20 duty to deal if somebody has an anthrax patent
21 that will -- could create an anthrax vaccine.
22 I don't think that the antitrust laws should be

1 just wiped aside and say that you can't get into
2 somebody's intent plus a detailed market
3 analysis. And I hope I wasn't the only one.

4 I think Chris earlier may have
5 suggested that he agreed in some limited
6 circumstances you can look at the patent holder's
7 intent in refusing to deal. So, Chris, I hope
8 you back me up here.

9 CHRIS SPRIGMAN: I'm not sure I said
10 that.

11 PAM COLE: Nice try, Paul.

12 CHRIS SPRIGMAN: I think this Kodak
13 opinion has become radioactive and it's a little
14 unfair. When the Court was talking about intent,
15 it was talking about an instruction to the Jury
16 and whether an instruction to the Jury that was
17 insufficient was nonetheless harmless because
18 Kodak's late in the game trundling forward in one
19 paragraph of the closing argument of an IP --
20 protecting investment in IP justification was
21 not basically credible.

22 It was a pretext. I'd like to be

1 charitable to this opinion and say it can be
2 reconciled with a better approach which is
3 not subjective intent so much as intent as
4 objectively probative of a strategy that had no
5 justification but for its exclusionary effect,
6 no profit maximizing justification but for
7 exclusion, by which again I mean to say that
8 although the intellectual property holder is
9 entitled to exclude and thereby collect a
10 monopoly rent -- and I think the Kodak Court did
11 say that -- that this reliance on its investment
12 in intellectual property as a justification was
13 in fact too feeble to rebut the possibility or
14 the likelihood that this strategy was in fact
15 something more than profit maximizing for a
16 monopolist.

17 It was in fact exclusionary past the
18 point where that was. So this reading of Xerox
19 requires a lot of interpretation and charity.
20 But I think it's available and it's somewhat
21 unfortunate language in the same way that the
22 Kodak language about the three exceptions to its

1 rule of per se immunity is unfortunate.

2 PAM COLE: Another Gallup poll
3 that I've been trying to take during the
4 presentations -- and I realize that Mark and Doug
5 still have some presentations to make -- is the
6 sentiment of the panel in terms of whether or not
7 there should be restrictions on refusals to deal,
8 antitrust restrictions.

9 And it seems to me that the sentiment
10 of the panelists is either that there should be
11 no restrictions whatsoever or if there should be
12 restrictions those restrictions should be very
13 limited. I think that's pretty much what
14 Professor MacKie-Mason stated when he presented.

15 And for those panelists who believe
16 that there should be some restrictions on a
17 unilateral refusal to deal albeit limited
18 restrictions, could you comment or discuss what
19 are some necessary predicate conditions, if you
20 will, in terms of when those limited restrictions
21 should apply.

22 I mean obviously a finding of market

1 power seems to be one that we would all agree on.
2 Are there any others that come into mind in terms
3 of when those limited restrictions on a refusal
4 to deal should apply? I don't know.

5 Professor MacKie-Mason, have you had
6 any ideas in terms of what you were thinking when
7 you said there should be limits? I assume from
8 that there should be instances in which you think
9 there should be restrictions.

10 JEFF MACKIE-MASON: I do although it
11 starts to ask me to be a lawyer to try to draw
12 these distinctions because I'm not sure we could
13 really make the argument clearly on economic
14 grounds. But I think it's more just a gut
15 instinct. Carl made the distinction between
16 conditional and unconditional refusals to deal.

17 That's a distinction I think is
18 important. But it also worries me a bit because
19 it's not -- even that there is still semantic
20 debate about what is conditional and what is
21 unconditional. You know, the refusal to deal
22 parts to ISOs is conditional on them being ISOs,

1 not owners of equipment.

2 There is a question of as long as they
3 don't use those parts to sell to another consumer
4 who could buy them as a several servicer, then is
5 that what we mean by conditional, unconditional?
6 I think some obvious things that are conditional
7 should be restricted. Tying is an example.
8 Ability to implement price fixing is an example.

9 I'm not convinced, but I think it is
10 a debate that would be good to have and wasn't
11 reached really in the Intel cases.

12 Whether or not course of reciprocity
13 should be restricted, you know, in that case
14 Intel withdrew its intellectual property arguably
15 allegedly to coerce firms to give away their
16 intellectual property for free, to grant Intel
17 zero price royalties.

18 So there we had a case of one firm
19 using the fact that it had market power plus some
20 intellectual property to coerce firms dependent
21 on intellectual property to give us essentially
22 their property rights, or at least that's what

1 the argument was.

2 It didn't really get a decision
3 because the Federal Circuit ruled the Intergraph
4 case on other grounds and the FTC case settled.
5 But I think course of reciprocity is another
6 case.

7 So these mostly are things that appear
8 to be conditional, but it's not entirely clear to
9 me what's conditional and what is unconditional.
10 I think that's a semantic issue. And from an
11 economic point of view I'm not sure the
12 distinction is that clear.

13 PAM COLE: Chris?

14 CHRIS SPRIGMAN: I think one other
15 limiting factor is that I would want to -- and
16 Professor Ordovery talks about this as the third
17 prong of his but-for test. I would want to
18 understand early what the mechanism is for
19 recoupment.

20 If there's no obvious mechanism for
21 recoupment, then query whether you should even
22 look further into the question of profit

1 sacrifice because the question of what is the
2 monopoly maximizing price is more I think
3 empirical, tough, intractable.

4 The other thing is imagine an instance
5 where a patented component for a machine is
6 being sold to licensees, being licensed to
7 licensees. And you had a situation where the use
8 of that component involved a lot of transfer of
9 know-how over time.

10 And the patent owner decides, well,
11 I'm going to identify the five or six companies
12 who are most likely to be able to take that
13 know-how and design around and limit the length
14 of my patent monopoly.

15 Now, that's probably unilateral
16 although I know there are a lot of theoretical
17 issues about what is unilateral and what isn't,
18 and I think we have to draw some lines. I think
19 I'd call that unilateral. But the effect of that
20 might be to suppress innovation that would
21 otherwise come along.

22 And the recoupment mechanism there

1 is quite clear. And maybe there is a profit
2 sacrifice in the process. So there is the kind
3 of case where, you know, if you could imagine the
4 facts you might get a relatively clear answer.

5 PAM COLE: Yes. Go ahead, Mark.

6 MARK WHITENER: But I guess then that
7 raises a couple of questions. Is it recoupment
8 if I make more money in servicing equipment
9 because I didn't sell my patented parts to ISOs?
10 Maybe a little bit harder question but

1 by that in the context of where the conduct is
2 essentially I'm not going to give up the patented
3 property.

4 PAM COLE: We're going to take a
5 ten-minute break in just a few minutes. I did
6 have one other question. But for the sake of
7 time I want to make sure that my fellow
8 government people did not have questions that
9 they wanted to ask. Gail or Sue?

10 GAIL LEVINE: I had a question for
11 Professor Wiley and Professor Klein about their
12 thesis. I understand that your basic point was
13 that many of these unilateral cases, unilateral
14 refusal to deal cases, in fact even the leading
15 ones can be described as metering cases.

16 But I gather from your recent
17 interchange with Professor MacKie-Mason that
18 doesn't go for all of them.

19 Can we use the insights of your thesis
20 about price discrimination in some way to help us
21 decide how to resolve the cases that aren't --
22 that don't boil down to metering cases?

1 JOHN WILEY: We didn't speak to that.
2 Let me give my co-author a crack at it. Our
3 thesis this morning dealt very specifically with
4 one particular justification for refusals to
5 deal.

6 And it really has a recommendation
7 explicitly for the FTC and the DOJ and for
8 private counsel representing people who may have
9 an antitrust problem that could be explained by
10 a price discrimination rationale.

11 I'm less confident than Professor
12 MacKie-Mason that the case law is so distant.
13 I think it's rather threatening in this area.

14 And I urge the government decision
15 makers here self-consciously to do what
16 government decision makers have done historically
17 in antitrust law, which is actively try to
18 influence the content of antitrust policy that's
19 generated by our Appellate Courts, particularly
20 the Solicitor General's office and the Supreme
21 Court, that are tremendously significant policy
22 decision makers here.

1 Now, how are these government decision
2 makers going to find the right case involving
3 price discrimination? Counsel can bring them to
4 them and say, you know, remember that guy Klein
5 and that guy Wiley; we've got that case.

6 We could really use some authoritative
7 help coming in and saying price discrimination is
8 an explanation that ought not to condemn this
9 refusal to deal.

10 Now, about other refusals to deal that
11 aren't explicable on those grounds, let me turn
12 it over to Ben Klein. But this is action items
13 both for the government and for private counsel
14 with cases that fit this description.

15 HEWITT PATE: May I ask just a
16 follow-up then?

17 JOHN WILEY: Sure.

18 HEWITT PATE: Do you think we should
19 be looking for opportunities to ask the Supreme
20 Court to overrule Brulotte and the Morton Salt
21 case which seem to me to be very readily
22 describable as metering cases? This is what I

1 was talking about when Ashish was going to the
2 podium earlier.

3 JOHN WILEY: I think that's an
4 extremely logical question. It shows that you
5 totally get our presentation that you're thinking
6 about those other cases. I'm going to give you
7 the classic appellate lawyer's response which is
8 that case isn't before us right now.

9 All I'm asking for is on the refusal
10 to deal point accept price discrimination as a
11 legitimate justification. It may well be that
12 there's implications that extend further.

13 But you could deal only with the case
14 on the issue presented today and still do some
15 real good. I'd be sympathetic to further
16 extensions. But that's not necessary for right
17 now.

18 GAIL LEVINE: Why is that a good place
19 to start as a -- as a sort of matter of advocacy?
20 Why is this particular area of price
21 discrimination case law the place to press first?

22 JOHN WILEY: Because we have a very

1 sharp conflict that somebody's got to fix sooner
2 or later. The Supreme Court and the Solicitor
3 General may have been convinced in the last go
4 around that the conflict wasn't sharp enough.

5 I think you've heard today
6 overwhelming response that, golly, there's a lot
7 of the private sector out there looking for
8 guidance on this point. The way to cure these --
9 this conflict we say is to understand the
10 underlying economics and to allow people to talk
11 about it without fear of automatic liability.

1 discrimination.

2 But they are -- in the cases that
3 we've looked at, they are generally very, very
4 limited, these alternative models that have
5 very limited applicability and where you're
6 foreclosing a crucial input to protect your
7 monopoly or to create a monopoly, in the Winston
8 case about leveraging into another market.

9 You need these conditions about large
10 economies of scale in the tied goods market where
11 somehow using this refusal to deal is going to
12 make it difficult for a new copier manufacturer
13 to come in and get personnel that could service
14 their machines.

15 And so -- and I think Jeff agreed
16 that these models have very, very limited
17 applicability.

18 What I think happens is it comes down
19 to the question of the relevant product market,
20 which is -- although Jeff says that's something
21 we all agree on, I think that really becomes the
22 empirical question on all these cases.

1 The question is: Is it useful to
2 define a market for the service of an individual
3 firm's products even if they have a very small
4 market share and abstracting from any kind of
5 opportunism or holdup problem, which is what is
6 done in all these cases?

7 And I guess what I would say first of
8 all in terms of these section 2 claims is price
9 discrimination, if you think that it is a
10 metering explanation, price discrimination should
11 be sufficient because it doesn't -- you don't
12 have the Ordovery/Willig standard anymore. No
13 profit is being forgone.

14 In fact they are getting extra short
15 run profit. So there's not this problem of
16 recouping it in the future. And this question of
17 recoupment I agree is an important question.

18 To an economist it's always recoupment
19 because you're not doing anything as a business
20 firm if you're not maximizing, you know, the
21 discounted value of your profit stream and
22 therefore you're getting some future wealth.

1 That standard only works if you're talking about
2 recouping it in future monopoly profit.

3 And that only works if you define an
4 arbitrary monopoly service market. So that's
5 what really this whole thing comes down to. Can
6 you define such a market? It's an empirical
7 question.

8 But I would say that in most of these
9 cases if you find out that it's metering you
10 should be home free in terms of talking about the
11 competitive process and predatory behavior. And
12 we shouldn't be out there -- and that's what I
13 didn't like about the debate that was going on
14 between you two.

15 Whether quantity goes up or goes down
16 from the discrimination of the metering I don't
17 think is important because the antitrust
18 authorities should be regulating the competitive
19 process.

20 We shouldn't be going into a
21 restaurant and saying, look, they are over
22 charging for the desserts and under charging for

1 the entrees and there's distortions and maybe the
2 quantity goes up and maybe the quantity goes
3 down, just as long as it's not predatory behavior
4 and the conduct is just part of a normal
5 competitive process, that should be the end of
6 the game.

7 JOHN WILEY: And, Ben, you and I
8 completely agree with that. We have some
9 continuing disagreement on the snappiest response
10 to the MacKie-Mason point. But we're reading off
11 the same sheet of paper.

12 PAM COLE: Okay. Let's take a quick
13 ten-minute break which means we should be back at
14 3:15. And then we're going to have Mark Whitener
15 and Doug Melamed.

16 (Recess.)

17 PAM COLE: Paul Kirsch has to leave
18 in about 15 minutes because he's flying out of
19 Baltimore. I don't understand why, but that's
20 what he's doing.

21 So Jonathan wanted to follow up on
22 something that Paul said. And then, Mark, if you

1 can -- I see you are well positioned to -- okay.

2 All right. So go ahead, Jonathan.

3 JONATHAN GLEKLEN: I thought to be
4 honest the most stunning thing that Paul said
5 is that if you have the patent on the cure for
6 anthrax and you refuse to license it and you do
7 it out of bad intent and you have a monopoly in
8 some relevant market for anthrax cures, that
9 that's an antitrust violation.

10 I can't tell you that innovation would
11 be reduced if we told -- you know. Pick a
12 valuable drug patent and said you know you have
13 to create generic competition, one time deal,
14 special circumstances. So to do the rule of
15 reason analysis I can't prove to you that the
16 result is procompetitive.

17 But I guess I would inquire whether
18 there is anyone else on the panel who thinks that
19 that's the right result. And I'd also say I
20 think there's case law out there that would
21 support that.

22 I mean if you are going to treat

1 patents like other IP, I think broad reading, you
2 know, of Colgate, you had an intent to maintain
3 your monopoly. You refused to license.

4 But I guess I would be surprised if
5 other people think that's the right result under
6 the antitrust laws, as opposed to some public
7 health regulation that Congress may pass if there
8 is a national emergency.

9 PAM COLE: Well, Paul is in the back
10 of the room. Does anybody else want to comment
11 on Jonathan's questions or comments? Go ahead,
12 Doug.

13 DOUGLAS MELAMED: I can't resist.
14 Clearly it's not an antitrust violation. But it
15 does seem to me there are tort principles that
16 would say that you cannot suddenly raise your
17 price to hold up the victims of the disaster,
18 that you have to sell it at what otherwise would
19 have been the market price. But I agree it's not
20 an antitrust principle.

21 ASHISH ARORA: Just a little
22 historical anecdote. At the end of World War II

1 chemical companies -- one prominent example
2 is ICI -- were compelled to license their
3 polyethylene compositional matter patent. It's
4 hard to figure out what would have happened if
5 they had not.

6 But it is true that innovation
7 proceeded very vigorously despite that. Now,
8 special circumstances and all that kind of stuff.
9 I find it troubling that people state as a matter
10 of principle that compulsory licensing will
11 result in bad things.

12 HEWITT PATE: May I ask a quick
13 question? If it's true that Colgate stands
14 for the general purpose proposition that the
15 refusal -- that the right to refuse to deal is
16 conditioned on the absence of bad intent, does
17 that mean either that the Ninth Circuit must be
18 right in Kodak or that the only way to say that
19 it's wrong is to say that intellectual property
20 is treated differently?

21 JEFF MACKIE-MASON: You're referring
22 to the language in Kodak that said absent a

1 purpose to monopolize a trader is free to choose
2 with whom he must do business?

3 HEWITT PATE: Right. I started by
4 saying if it stands for that.

5 JEFF MACKIE-MASON: I'm not sure that
6 purpose meant subjective motive.

7 JONATHAN GLEKLEN: I don't know that
8 the only inquiry there is intent, but I think it
9 affects the relevance. I think Colgate says if
10 you're not -- if you don't have a monopoly and
11 you're not keeping a monopoly you can refuse to
12 deal.

13 But if you do have a monopoly and
14 you're keeping the monopoly as a result, you
15 don't have a right to refuse to deal. Maybe
16 Colgate is just wrong. Maybe Colgate is bad law.

17 PAM COLE: Okay, Mark. You've been
18 very patient.

19 MARK WHITENER: I always thought
20 Colgate was most often cited for the proposition
21 that you can decide unilaterally what to do with
22 what you own. And I read that language as sort

1 of a Court saying we never say never.

2 I mean there is a temptation in this
3 area of antitrust to sort of carve out exceptions
4 or to give yourself a little wiggle room which is
5 in my mind part of the problem.

6 Okay. I'm Mark Whitener. I'm
7 antitrust counsel at GE. And my perspective is
8 as one who has been in antitrust enforcement. I
9 actually supported some cases that some of the
10 dais opposed. And some of them involved
11 intellectual property.

12 So I think there is an important role,
13 a very critical role that antitrust plays in the
14 economy generally and in intellectual property in
15 particular.

16 But I do have some thoughts on this
17 unilateral or I think it's fair to assume for
18 purposes of my remarks unconditional refusals
19 to deal or refusals to license. And I should
20 probably make it clear that these views are mine
21 and not necessarily those of GE. I don't have a
22 PowerPoint presentation either. But.

1 I have two very simple bullets if you
2 want to visualize them on the screen. What's
3 wrong with the state of the law today, and what I
4 think the agencies can do about it partly as a
5 process of having these hearings and giving some
6 greater policy guidance going forward. Now, let
7 me address the state of the law briefly.

8 And it's been discussed at length
9 today so I won't go into a lot of detail. But
10 there are really two issues I think, two aspects
11 of the Kodak decision that cause great confusion.

12 And in particular my perspective is
13 that of a counselor to one company in particular
14 that has long been an innovator and an owner of
15 intellectual property.

16 And those two aspects of the decisions
17 or fundamental flaws you might say are first this
18 artificial subdivision of IP rights into multiple
19 markets for purposes of applying the law of
20 unlawful extension of IP rights from one market
21 to another.

22 And the other is this analysis,

1 emphasis on subjective intent and actual versus
2 pretextual motivations for refusal to license.

3 Now, on the first point, the Ninth
4 Circuit basically said that a unilateral refusal
5 to deal can be unlawful simply because the patent
6 rights at issue can be subdivided into multiple
7 antitrust markets, which is often going to be
8 nothing more than saying as I think someone
9 pointed out this morning, there is a market for
10 the intellectual property itself.

11 And there is -- there are one or more
12 end uses for that intellectual property. There
13 may be many.

14 And as I'll come back to in a moment,
15 how many markets a particular innovation can
16 affect or in how many end uses it can be
17 exploited is something that's probably going to
18 be unknown and unknowable to the innovator at the
19 time they are making the initial investment.

20 So under this approach virtually any
21 time that the subject matter of the patent, the
22 claims, the technology, the innovation that's

- 1 claimed by the patent has more than one end use
- 2 or can be categorized as falling into more than

1 are not going to be able to know often when
2 you're innovating, when you are making the
3 investment or trying to decide how much to
4 invest, how you will ultimately exploit, what
5 business plan you will use to go to market with
6 the technology, whether you're going to be
7 dealing with one, two, three, or more antitrust
8 markets.

9 And the other thing I want to say
10 about this and the other Ninth Circuit Kodak
11 issue that I'm going to talk about is what we're
12 dealing with here fundamentally is uncertainty.
13 It's of course a problem if liability is imposed
14 based on these theories.

15 As Doug and others have pointed out,
16 not a lot of cases actually end up with damage
17 awards. Some do. But more importantly the
18 specter of liability and the fact that liability
19 turns on these very difficult if not unknowable
20 questions creates a chilling effect.

21 It creates uncertainty which in turn
22 undermines the rationale for and the degree of

1 investment in innovation. Now, you know, how
2 much does it do that?

3 And Pam gave me permission sort of to
4 breach the lunchtime privilege by describing a
5 conversation we had at lunch today in which she
6 talked about a very interesting case she handled
7 when she was a young lawyer and was working in
8 Colorado and went out and successfully prohibited
9 springtime hunting of female bears who had cubs.
10 Is that basically right? Close enough.

11 PAM COLE: That's right.

12 MARK WHITENER: And one of the
13 arguments she faced from the Court was, well,
14 do you have any empirical evidence of how many
15 bears, you know, how many fewer bears if any we
16 have because of this -- because of this policy or
17 how many bear cubs are being killed because their
18 mothers are hunted?

19 And she basically said, well, you
20 know, we may not have a whole lot of evidence,
21 but if you are saying that there is no loss,
22 tell that to the dead bear, the point being we

1 shouldn't place the burden on the IP owners or
2 on the innovators to prove the degree to which
3 innovation is chilled when there is essentially a
4 forced diffusion of the technology by virtue of
5 the antitrust laws.

6 So I think that directionally it seems
7 to me clear that innovation is reduced when the
8 ability to reap a return on the investment is
9 diminished and when uncertainty is introduced

1 objective. And legally and analytically the
2 distinction is meaningless. From a counseling
3 standpoint, try to explain to a business person
4 the difference between those two things.

5 What you explain is of course that
6 it's always a good idea to create documents that
7 emphasize the positive and that don't talk about
8 harming competition and cutting off air supply
9 and destroying the bad guys. That's just common
10 sense.

11 But it shouldn't be the ultimate or
12 a critical issue in determining whether there's
13 antitrust liability. And then once that fact --
14 and clearly that is a fact, what was the intent,
15 what was the real intent, what was -- or was it a
16 pretext.

17 Once that becomes an issue, an element
18 of the offense, then it is a question for the
19 Jury. And as John said, you know, if you are
20 before a Jury you face the prospect, some
21 probability, even if it's low, of liability,
22 potentially quite large damages if you look at

1 the array of arguments that might be made.

2 It creates a settlement value and it
3 creates very real effects even if very few cases
4 actually get to the point of substantial damage
5 awards. The other thing I'd point out is that
6 the magnitude of the risk increases as the value
7 of the intellectual property itself increases.

8 That is to say all else being equal a
9 more valuable, a more important innovation is
10 more likely I think to be susceptible to the
11 kinds of arguments that at least under Kodak can
12 create liability, all else being equal. More
13 likely I would say to be found to create or
14 confer market power.

15 More likely to be something that a
16 competitor will say that they need in order to
17 compete with you. So this is precisely the
18 situation where the innovation is the most

1 been met with universal approval. It's fair to
2 say I suppose even by the successful litigants.
3 So I'm not going to defend Xerox's analysis.

4 I do want to though respond briefly to
5 what I see as a couple of the camps into which
6 criticism of Xerox falls. One is that it got it
7 wrong, that Kodak is either right in the result
8 or in the analysis. I don't agree with that.

9 Another is that the Xerox Court
10 in this dictum inaccurately or incompletely
11 described the so-called exceptions to the general
12 right to refuse to deal. That dictum can be
13 criticized as confusing, inaccurate, or
14 incomplete. I agree with that.

15 But the criticism I want to respond to
16 and I want to spend the most time on now for a
17 couple minutes is the idea that -- and this was
18 expressed in the SG's brief in the case opposing
19 cert. -- is that, look, as a general matter we
20 should refrain from creating categorical sort of
21 exceptions to the antitrust laws or categorical
22 rules of legality or immunity.

1 Those are disfavored. We should look
2 at cases on a case-by-case basis. We should look
3 to see whether particular conduct runs afoul of
4 some theory of competitive harm. Now, this
5 sounds like a very flexible approach, and so
6 therefore it might be seen to be a reasonable
7 approach at first blush.

8 But I think when applied to unilateral
9 or unconditional refusals to deal that it's wrong
10 for several reasons. First of all, just the fact
11 that section 217(d) of the patent act does appear
12 to give -- to be a Congressional expression of
13 treating at least patents differently than other
14 forms of property.

15 But, second, you know, I think
16 you have to look at the fact when critics of
17 categorical legality point to situations where
18 they think liability should be imposed, often
19 I think you can if you look carefully at those
20 arguments you conclude that they involve some
21 form of conduct other than a pure or
22 unconditional or unilateral refusal to deal.

1 That might well be analyzed under existing and
2 much more widely accepted antitrust theories.

3 The other problem with this criticism
4 of Xerox, that it improperly creates sort of
5 immunity for a certain category of conduct, is
6 that the critics don't -- I think still have not
7 successfully articulated a theory of violation
8 that fits within the bounds of antitrust analysis
9 as we sort of commonly look at it today at least
10 in this country.

1 But each one it seems to me at least
2 so far as what I've heard from proponents of some
3 duty to deal in IP rights really fails in going
4 element by element and saying, okay, what is it
5 about the pure, unconditional refusal that is the
6 exclusionary conduct.

7 How do we measure this predatory or
8 anticompetitive effect, and what do we take into
9 account on the procompetitive side? Is the
10 desire to extract every last dime of return from
11 the intellectual property right a legitimate
12 justification?

13 Or is that itself if characterized the
14 wrong way somehow viewed as exclusionary? And
15 that's all before you get to the question of
16 remedy. And when you get to the question of
17 remedy I think as Carl and others have said, I'm
18 not sure we really want to ask the agencies and
19 the Courts to be regulators of price.

20 And even if we're talking about a
21 simple nondiscrimination order it's really not
22 so simple.

1 So what I think we really need to do
2 is focus on antitrust as an enforcement, a law
3 enforcement regime in which we only prohibit
4 conduct or require a remedy when we have a
5 clear theory of harm that has -- you know, it's

1 that took a somewhat different view.

2 So it may be appropriate for the
3 agencies as an outgrowth of these hearings to go
4 back and resolve this question in a way that
5 everybody can agree is clear and that everybody
6 can understand. Thanks.

7 (Applause.)

8 PAM COLE: Okay, Doug. And, Mark,
9 happy 35th birthday.

10 DOUGLAS MELAMED: I'm going to focus
11 on one question, but there will be implications
12 for others.

13 The question I'm going to focus on is:
14 Is there something about intellectual property
15 that should cause it to be treated differently
16 for purposes of refusal to deal violations under
17 the antitrust laws from other kinds of property?

18 Now, the first thing that I did when I
19 began to think about this question was to look at
20 it as a legal question. What's the law? The law
21 is quite clear. Immunities from the antitrust
22 laws are disfavored.

1 One should look either for clear,
2 express Congressional intent to immunize conduct
3 or for repugnancy between some other body of law
4 and antitrust. And without that the antitrust
5 laws ought to prevail because of their enormous
6 importance to our economy.

7 And if you go through that legal
8 exercise which I think few of the cases for
9 understandable reasons have not gone through, you
10 find that there is no legal basis for an immunity
11 for intellectual property law. The IP statutes
12 do not provide for antitrust immunities.

13 While it is true that they gave what
14 appear to be unqualified grants of authority to
15 license and exploit and use the property and so
16 forth, the language and the legislative history
17 I think makes clear that that is intended to
18 do more than to ensure that the owner of
19 intellectual property rights will have rights
20 that are not inferior to those that we normally
21 associate with the owner of tangible property.

22 The legislative history of the 1998

1 amendments which refer to the use of refusal to
2 deal as a defense I think demonstrates the same
3 thing.

4 Similarly I think if one looks at the
5 Supreme Court cases, some of the old cases that
6 used broad language about the rights of
7 intellectual property holders, one finds that
8 they were using either the language that was
9 contemporaneously used to describe the rights
10 of the holders of tangible property or that
11 in context they quite clearly meant that
12 intellectual property rights should not be
13 inferior to those of the rights of other --
14 rights of owners of other kinds of property.

15 So I think using traditional legal
16 tools while arguments can be made on both sides
17 I'm persuaded that by far the stronger argument
18 is that there really is not a good legal basis
19 consistent with the general proposition that
20 immunities are disfavored for finding an
21 immunity.

22 But I'm willing to grant that because

1 no one seems to care about that -- and by no one
2 I mean the cases, Supreme Court and lower Court
3 cases -- that maybe like those cases we should
4 jump immediately to the policy analysis sort of
5 tied to what was said and ask the question of
6 whether it makes good sense to have a special
7 immunity.

8 I don't think you can get there by
9 looking at the policies of the intellectual
10 property laws. To be sure they are intended to
11 create rewards to innovation by giving rights of
12 ownership to the innovator. But those rewards
13 are not intended to be infinite. They are not
14 intended to be maximized.

15 We know that from the face of the
16 intellectual property laws. They are limited in
17 duration. They contain within them doctrines of
18 patent misuse and copyright fair use. They
19 prohibit tie-ins and other things more broadly
20 than do the antitrust laws.

21 So it is clearly not a principle of
22 intellectual property law that the owner of

1 intellectual property is entitled to maximize his
2 returns, to use his property in whatever way
3 maximizes his profits.

4 And so one I don't think can assume
5 that there is an incompatibility between an
6 antitrust regime that might prevent the IP holder
7 from doing what he wants to do and the values and
8 objectives of the intellectual property laws.

9 The real issue I believe is a question
10 of whether antitrust analysis is up to the job
11 of protecting the legitimate interests of
12 intellectual property while at the same time
13 serving its own interests in promoting
14 competition.

15 Now, we're dealing when we talk about
16 refusals to deal with that branch of antitrust
17 which are the offenses of exclusion by which
18 one refers to offenses in which one or more
19 defendants seeks to weaken or exclude a firm that
20 would otherwise be its rival and thereby getting
21 market power to the detriment ultimately of
22 consumers or suppliers.

1 And although there are wrongly decided
2 cased and old cases and inconsistent cases, I
3 think there is an emerging consensus that the
4 principle -- the basic antitrust principle
5 applicable in all cases involving exclusion is
6 something very similar to the Ordoover/Willig
7 predation principle.

8 It's expressed differently in
9 different cases. But I think it comes down to
10 something like this.

11 Did the defendant engage in conduct
12 that didn't make business sense for it or that
13 was not profitable for it, but for the tendency
14 of the conduct to weaken or exclude rivals and
15 thereby enable the defendant to gain additional
16 market power that it would otherwise not have,
17 and to recoup its investment by exercising that
18 market power and earning supercompetitive profits
19 it would not otherwise be able to earn.

20 I think that is -- that principle
21 explains frankly both the section 1 and the
22 section 2 violations that have exclusion as their

1 attribute. Tying would be an example of that.

2 The conduct in which Microsoft
3 engaged, predatory pricing, all of that kind of
4 conduct I think can be subsumed at some level of
5 abstraction under that principle.

6 Now, that's a very conservative
7 principle. It is a conservative principle
8 because it means that in order for a firm to
9 violate the antitrust laws in an offense of
10 exclusion it has to engage in conduct which in
11 a static sense is not efficient at the margin.

12 In a static sense the costs of the
13 conduct are greater than the benefits of the
14 conduct, and it's welfare reducing without regard
15 to the welfare costs of recoupment.

16 And it's a conservative test because
17 one can surely imagine situations in which a firm
18 might for example invent a new process, patent,
19 lower its production costs by 5 percent below
20 those available elsewhere in the industry, drive
21 its rivals out of business, raise its prices by
22 50 percent, make huge profits.

1 No one will enter because they know if
2 they ever did, because this guy owns the process
3 patent he'll undersell them. And long run
4 welfare is diminished. And yet in our country,
5 in the United States, perhaps not in Europe, I
6 think we say that's okay.

7 We want to have a very conservative
8 law to guard against false positives, to guard
9 against too much government intervention into the
10 economy. And the defendant wins because his
11 process patent was skilled foresight in industry.
12 It was not -- it didn't violate the predatory

(was inefficill (ductD (ight in industry.) 5 TDs iic seto 10 we

1 by defendants who argue for what I will call
2 formalistic rules to guard against false
3 positives in the enforcement of the antitrust
4 laws. The Microsoft case was a wonderful example
5 of this for depending on how you count them eight
6 or ten such arguments.

7 Microsoft argued that product design
8 should be safe harbor because even though we can
9 all imagine a situation in which product design
10 might be anticompetitive in the sense that I've
11 used that word Microsoft said Courts are too
12 likely to get it wrong. There are too likely to
13 be false positives. There should be safe harbor.

14 Microsoft argued that in high-tech
15 dynamic industries there should be different ways
16 of measuring market power to guard against false
17 positives. They argued that there should be
18 mechanical measures for exclusive dealing.

19 And the government argued in that case
20 that there should be -- by the way, this is a
21 little different -- formalistic rules that could
22 condemn tying without actually proving that you

1 satisfied the predation test.

2 The Court of appeals in Microsoft
3 and I think in an exquisite expression of the
4 emerging consensus in antitrust law rejected
5 every single formalistic argument, plaintiff
6 tying argument and padded Microsoft defense
7 arguments and said, no, we're going to look at
8 every allegation of exclusionary conduct from the
9 bottom up looking at the facts and asking the
10 question, is this conduct was conduct that made
11 no business sense or served no legitimate purpose
12 or wasn't profitable but for its tendency to
13 exclude a rival, generate additional market
14 power, and permit anticompetitive recoupment to
15 the detriment of trading partners.

16 I believe that was the correct
17 analysis. And the question is whether there's
18 any reason why that analysis shouldn't be used in
19 a refusal to deal case, and if there isn't why
20 there is any reason why it should be used in most
21 refusal to deal cases but not in refusal to deal
22 cases involving intellectual property.

1 I believe that the law is sufficiently
2 tractable, and the tools and investigation
3 notwithstanding the fact it won't be perfect are
4 sufficiently suitable that we can use that
5 predation test in a refusal to deal case so that
6 if Microsoft, for example, had simply refused to
7 give its APIs to Netscape and had used that
8 particular device to do in Netscape we would have
9 been able to say I don't care if it has the label
10 refusal to deal.

11 That sounds to me like anticompetitive
12 conduct. And we could have analyzed it the way
13 the Court analyzed the other conduct that was
14 alleged and found to be anticompetitive in the
15 Microsoft case. So the question then is what
16 about IP. Should that lead to a different
17 result?

18 Well, it seems to me the answer there
19 is no because there's nothing about IP that
20 makes the refusal to deal test any more or less
21 intractable. And there's nothing about IP that
22 requires any greater protection for the rewards

1 to skillful foresight in industry. Consider the
2 AT&T case.

3 Would that have been a -- and assume
4 for the moment that Professor Baxter was correct,
5 that that was a great antitrust case. Should the
6 result in that case have been any different if
7 AT&T's interfaces had been patented? And MCI
8 could not have plugged into the AT&T system
9 without getting a patent license.

10 Would it make any sense to say that's
11 a different case because there's intellectual
12 property there? Would it make any difference to
13 say in the Microsoft case that Microsoft has to
14 disclose its APIs except if they are copyrighted
15 and then it doesn't have to disclose its APIs?

16 So the problem with an exception for
17 intellectual property, one of them is you are
18 going to have false negatives. You're going to
19 have those occasional serious refusal to deal
20 problems uncorrected because you happen to have
21 intellectual property.

22 A second effect of a formalistic

1 subtle threat that was so effective that
2 everybody complied with the wishes of the
3 manufacturer.

4 And the third effect it seems to me
5 of having a safe harbor for intellectual property
6 in the refusal to deal area is that it will
7 directly, explicitly, and foreseeably undermine
8 the purposes of the intellectual property laws.
9 It will do that by creating incentives to distort
10 the innovation process.

11 Imagine you are a lawyer in a world in

1 intellectual property community have.

2 I don't think we're going to have many
3 plaintiffs winning refusal to deal cases. I
4 think once they learn that the strike suits will
5 dissipate as they have in other areas of
6 antitrust.

7 But I don't think we should throw out
8 of the arsenal of antitrust the opportunity to
9 bring a refusal to deal case, to bring an
10 exclusionary case against arguments that this is
11 a refusal to deal as opposed to some other kind
12 of exclusion.

13 This is intellectual property as
14 opposed to some other kind of property. Let's
15 get rid of the formalism. Let's let antitrust in
16 this area as most other areas treat exclusionary
17 practices from a fact based, ground up
18 perspective without formalistic rules and
19 safe harbors.

20 (Applause.)

21 HEWITT PATE: Thanks, Doug. I expect
22 that will prompt a few questions. Maybe I'll

1 start with one which is about the statute, the
2 271(d)(4) point. I take your point with respect
3 to the general thrust of the 1998 amendments
4 being to put intellectual property on the same
5 footing.

6 But the amendments have a provision
7 that relate to conditional licensing and would
8 seem to immunize it from challenge unless a
9 plaintiff can show market power. And so in that
10 context I think it's clearly bringing IP on to
11 the same footing away from a less favorable one.

12 But yet that part of the statute
13 exists side by side with 271(d)(4) which seems
14 to give a much more uncategorical approval to
15 exclusive -- well, to blanket unconditional
16 unilateral refusals to license.

17 Why isn't it a better reading to say
18 the statute to refute this is greater, includes
19 the lesser argument that, say, in the Townsend
20 case people are trying to run to defend
21 conditional licensing practices, but that really
22 there is a difference where the refusal is a

1 blanket refusal, an unconditional refusal.

2 DOUGLAS MELAMED: That is the toughest
3 question for my position. I agree. I'd just
4 say two things about it. One, it doesn't say
5 antitrust immunity. So on its face however
6 broadly you read it, it does appear to be limited
7 to IP defenses and the like.

8 Secondly, I think there is some
9 reason from the legislative history to reach the
10 conclusion that I reached. But rather than try
11 to bluff you into thinking I remember what those
12 arguments are, let me just refer you to the paper
13 that was handed out here.

14 HEWITT PATE: Other comments?
15 Questions? Responses?

16 CHRIS SPRIGMAN: I guess I'd ask Doug
17 why he thinks that Aspen and Otter Tail can be
18 read as incorporating the Willig/Ordovery test?
19 If in fact they did, I might be more comfortable
20 saying the same rules apply. But, you know,
21 Aspen says excluding somebody on the basis of an
22 efficiency.

1 And you don't have an efficiency
2 defense for a refusal to license generally.
3 Generally it's, hey, they are my competitors. I
4 don't want to do business with them because if I
5 license I'm going to be able to sell my drug for
6 four dollars, not forty dollars.

7 DOUGLAS MELAMED: Aspen may be a nutty
8 case on the facts. But Aspen did think that the

1 the Areeda Hovenkamp treatise as being a
2 perfectly -- well, a pretty straightforward
3 justification of the entire analysis, rather than

1 or not.

2 I think we can all agree that there
3 are some kinds of practices that would in fact
4 implicate exclusive dealing or tying or some
5 other conduct that could be examined under the
6 antitrust laws.

7 Second, you said I think that the
8 ideas -- the principles underlying the IP laws
9 are somehow themselves subverted if you have sort
10 of broad based protection for a refusal to deal.

11 Mr. Polk this morning I think made a
12 point that I think goes the opposite direction,
13 which is that the principles of the antitrust
14 laws are to some extent subverted if you find
15 or leave open the possibility of liability for
16 a refusal to deal because what happens in the
17 absence of a right to demand access to
18 intellectual property is people find other ways
19 to skin a cat.

20 They innovate. They develop -- they
21 invent around or they come up with an entirely
22 new approach.

1 And then finally in terms of sort of
2 the analytical standard that you described, I
3 still have trouble understanding in what case,
4 under what facts a refusal to share intellectual
5 property standing alone could be a problem.

6 I can see how it might be described
7 as a problem under your short run -- well, under
8 your sacrifice of profits for anticompetitive
9 gains. But I'm not sure how that applies
10 in fact.

11 If I'm sacrificing profits in some
12 sense now by refusing to sell parts to ISOs
13 because it might be as a matter of fact that
14 if there were more people out there providing
15 service my equipment revenues might go up.
16 Somebody could argue that.

17 But what I really don't want to do is
18 have the ISO take my parts, have that facilitate
19 their service, and have them learn how to be a
20 better service competitor. And I don't want that
21 to happen. Am I justified in preventing it?
22 Ashish?

1 ASHISH ARORA: This goes to the second
2 of Mark's points, and it's something I've been
3 trying to puzzle over. There seems to be -- and
4 maybe Jeff MacKie-Mason said this earlier. There
5 are two ends of the table. From that end I hear
6 conditional refusals are bad or could be bad.
7 From this side I hear price discrimination.

8 And I'm trying to figure out whether
9 these two statements -- that price discrimination
10 is if not good, at least legitimate. I'm
11 wondering if these two are in conflict or not.
12 So it is as much a question for the two ends of
13 the table as a kind of comment.

14 BENJAMIN KLEIN: I think they are two
15 separate concepts. I don't think they are in
16 conflict. I mean you can unilaterally set up a
17 metering arrangement that's not conditional on
18 anything.

19 ASHISH ARORA: Price discrimination
20 means you are charging different prices to
21 different people.

22 BENJAMIN KLEIN: Yes.

1 ASHISH ARORA: Conceivably that's
2 conditioned on something. How are your
3 differentiating those people? And so I'm not
4 sure. Anyway, this is as much for my education
5 as anything.

6 BENJAMIN KLEIN: Probably the lawyers
7 should answer it because this whole thing about
8 what is conditional and what an agreement
9 consists of I always find somewhat fuzzy. But
10 I don't see any conflict.

11 CARL SHAPIRO: I'm at this end of the
12 table, but I'm not a lawyer. But I did bring
13 up -- emphasize the conditional. It seems to me
14 that price discrimination is basically a method
15 of you're trying to maximize the value of your
16 property.

17 This whole issue of conditional -- and
18 I and Mark had mentioned tie-in and exclusive
19 dealing or selective licensing. I think of that.
20 And you are trying to set up incentives, let's
21 say, that will exclude competitors, that will
22 make -- by having conditions.

1 You can have my property if you agree
2 not to deal with a competitor. Well, that's
3 another barrier to the competitor. That's
4 completely separate than price discrimination
5 which is here is how I choose to price my stuff.
6 Deal with whoever you want but these are my
7 prices. It's just orthogonal.

8 JONATHAN GLEKLEN: I think the problem
9 in determining what's a conditional refusal to
10 deal with what's a unilateral refusal to deal
11 could arise in the following example.

12 A licensor goes out and grants a whole
13 bunch of companies short-term licenses and then
14 at the end of the term it refuses to relicense

1 CARL SHAPIRO: If I may, I won't use
2 these terms unilateral versus agreement. It
3 seems to me that is conditional. I mean you just
4 said everybody knows it's conditioned. Hey, the
5 reason I'm not granting you a license is because
6 you're dealing with this other guy who is my
7 competitor.

8 Now, we might have factual disputes
9 about whether that's what's going on. I think
10 that's unavoidable because the guy might say you
11 didn't give very good -- there may be some other
12 set of reasons and that may or may not be a smoke
13 screen for in fact you're dealing with my
14 competitor.

15 But in your hypothetical where
16 everybody knows what's going on, that's basically
17 equivalent economically to an exclusive licensing
18 regime. It's not in the agreement that you have
19 to be exclusive. But everybody understands if
20 you are not I'm not going to re-up you. So I
21 think that's straightforward.

22 That's conditional. That could well

1 be a problem. And of course the remedy for that
2 is not to get into regulating the prices but to
3 say, no, that's not a legitimate -- may not be a
4 legitimate basis for refusing to deal.

5 BENJAMIN KLEIN: I mean de facto it is
6 conditional the way I understand your example, or
7 I guess your example. But we know that it
8 doesn't meet the Monsanto criteria. And in the
9 real world people know a lot of things.

10 And I don't think we want to infer
11 agreements by figuring out what is in people's
12 minds. I think we need some objective criteria
13 about what it is -- I sound too much like a
14 lawyer. I should stop.

15 DOUGLAS MELAMED: You're a good lawyer
16 though.

17 CHRIS SPRIGMAN: Let me just respond
18 to that though. It's pretty clear that the
19 patent gives you a right to give field of use
20 licenses. And I think you undercut that if you
21 say I can't unilaterally refuse to license people
22 who are going to practice it in the field of use

1 that I prefer to maintain for myself.

2 So Xerox's photoreceptors in the
3 claims they note that the -- I'm sorry, the fuser
4 rolls, note that the patented coating can also be
5 useful in the field of cookware.

6 So Xerox says I'm going to license my
7 patents to people who make cookware and I'm not
8 going to license my patents to people who want to
9 make parts or to people who want to use the parts
10 to compete with me. That's a selective
11 licensing.

12 Are you saying that -- you know, if
13 the cookware manufacturer gets into the fuser
14 roll business and I terminate his license or I
15 don't renew it that that's anticompetitive?

16 CARL SHAPIRO: No. At least -- if
17 you're looking at me the answer is certainly not.
18 I'm not in any way trying to attack field of use
19 restrictions. It's a question again about
20 whether other competitors are excluded through
21 arrangements with third parties that may lock
22 them up.

1 HEWITT PATE: Yeah. I don't think --
2 well, is there anyone on the panel who has
3 understood the discussion today to indicate that
4 all conditional refusals are unlawful? Because I
5 think what we have been saying is that -- or what
6 I've been hearing is that perhaps unconditional
7 refusals are on a different footing.

8 But in that discussion I haven't heard
9 anybody indicate that conditional refusals are
10 bad necessarily because they are conditional.
11 Other comments? Questions?

12 CARL SHAPIRO: I just want to throw in
13 one more thing. Doug, I just don't get how your
14 whole approach is really workable. It seems to
15 me you want to do some inquiry about whether
16 these effects were anticompetitive and whether
17 there was sacrifice.

18 And I just don't know what that --
19 what I think of as a standard case where I'm not
20 licensing to you because if I do you're going to
21 be a stronger competitor and that's going to
22 lower prices and that's going to reduce my return

1 and I just don't want to do it. That's not going
2 to happen right away.

3 It's going to happen over time. So
4 what are you going to do with that case? You are
5 going to do what? You are going to do some long
6 run, short run trade-off? You're going to --
7 what are you going to do?

8 DOUGLAS MELAMED: Well, wait a minute.
9 As you stated, those words would have been
10 Microsoft's defense to a refusal to let Netscape
11 use its APIs.

12 And yet, Carl, I have a hunch that you
13 would find a violation if Microsoft had refused
14 to let Netscape use its APIs because you would
15 have said what conceivable efficiency purpose,
16 what benefit to consumers, what profit
17 enhancement other than driving a competitor out
18 of business and raising entry barriers or
19 increasing market power is going on here.

20 HEWITT PATE: I'm not sure if Carl's
21 name tag is really still up or not.

22 CARL SHAPIRO: You should be careful

1 about your hunches for one thing. But maybe
2 you're saying then if there was an ongoing
3 historical pattern of disclosing the APIs then
4 they might want to continue it.

5 That seems to me different than saying
6 just because somebody has interfaces and they are
7 valuable that they should be disclosed. So now
8 you have retreated it seems to me into the
9 category of ongoing patterns of dealing rather
10 than a broader principle of imposing duties when
11 there is not ongoing.

12 DOUGLAS MELAMED: I didn't mean to say
13 as a matter of principle. I'm saying plaintiff
14 has an evidentiary burden. He has to prove that
15 this doesn't make any sense. And obviously if
16 there were an ongoing patent it would help him.
17 But I wouldn't get there as a matter of
18 principle.

19 MARK WHITENER: Well, I have no priors
20 on Microsoft. So it doesn't make any sense.
21 What does that mean? What you just described
22 sounded to me like a pure simple refusal to share

1 intellectual property which I think as an
2 actionable offense falls flat.

3 And I thought Carl made the -- in his
4 point, counterpoint with himself on some of the
5 issues -- the side that won out seems to me was
6 the side that said you ought to be able to
7 re-examine your decision making.

8 That is to say, the fact that you
9 might have let something out of the bag before
10 and licensed it or shared it shouldn't prevent
11 you from later re-evaluating that decision. It
12 may have some consequences in the market that
13 people design around, lock in, whatever.

14 I'm not saying it's irrelevant. But
15 it seems to me that for the most part you ought
16 to be able to re-examine that question and make a
17 new decision later based on the facts before you.

18 CHRIS SPRIGMAN: Doug, was your
19 Microsoft hypothetical dependent on leveraging
20 and that the operating system was going to be
21 different from whatever market it is they were
22 not disclosing the APIs?

1 Because if not, I don't know how it's
2 any different from refusing to license my patent

1 As for the Microsoft story, I was
2 imagining the very same violation that every
3 Judge has looked at found. A very conservative
4 Court of Appeals found unanimously, and that is
5 Microsoft sought to do in a competitor because
6 the competitor threatened to lower barriers to
7 entry to compete with its desktop monopoly.

8 And all I'm suggesting is if they had
9 chosen instead of the variety of illegal things
10 they chose an otherwise economically irrational
11 decision not to let this particular competitor
12 have access to its APIs.

13 And the fact finder could conclude
14 as the fact finder did with all the things that
15 Microsoft actually did that that refusal also
16 served no legitimate purpose and was intended
17 solely to insulate its desktop operating system
18 from competition, that that should state a claim
19 under the antitrust laws. That's all I'm saying.

20 BENJAMIN KLEIN: I think that what you
21 are saying is that the once the market power gets
22 to a significant level there is a different

1 burden. I mean you're really moving to an
2 essential facility doctrine here. I know we hate
3 that term. But somehow the APIs are an essential
4 facility.

5 That is the only way you can make
6 sense of the argument because it does seem like
7 legitimate business justification. Why should I
8 license a competitor? I mean it has nothing to
9 do with Ordoover/Willig. You just don't want to
10 license a competitor and create competition.

11 So I think you really are talking
12 about an essential facility. And once you
13 become a monopolist you might have additional
14 obligations under the antitrust laws. I mean
15 that's it. But I don't think it fits your
16 framework.

17 HEWITT PATE: Okay.

18 CARL SHAPIRO: Well, we've cleared
19 that up.

20 HEWITT PATE: Now that we're cleared
21 that up, I guess we're drawing to the end of our
22 time. I'm not sure I'm in a position to sum up

1 accurately, particularly having gone AWOL for an
2 hour or so.

3 But we have heard a lot of things,
4 broad agreement that the CSU dicta is too broad
5 and doesn't necessarily accurately reflect the
6 state of the law at least as it relates to
7 conditional refusals.

8 I think broad agreement with one
9 exception that the pretext or subjective analysis
10 doesn't really add anything to this. Some
11 disagreement on whether IP is in some ways on a
12 different footing than other property.

13 A consensus that unilateral refusals
14 to deal are subject only to very narrow antitrust
15 liability all around the table, but maybe a real
16 disagreement about how narrow is narrow when you
17 get down to it, and some objections to whether
18 there should be liability at all chiefly because
19 administrability and incentive reasons, perhaps
20 because of the uncertainty created by private
21 litigation.

22 We've heard about other possible

1 approaches revolving around price discrimination
2 and otherwise. And I'm sure this is food for
3 further thought and debate.

4 But I'd like to thank the organizers
5 again and especially thank the panel members for
6 what I think was a great presentation and invite
7 all of you to be back tomorrow for settlements in
8 the next installment of the hearings. Thanks
9 very much.

10 (Conclusion.)

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