The Federal Trade Commission Workshop on

patentee is able to exercise increased market power in licensing negotiations because its patented technology has been incorporated into a standard.³ The adoption of technical standards can generate switching costs that change the competitive landscape for an industry. After a standard is adopted, firms may begin to make irreversible investments tied to the adopted standard. Moreover, collaborative standard setting can be a lengthy process that requires SSO members to reach consensus on a large number of complex technical issues. Changing a standard after the fact can add additional delay that slows the introduction of new products, resulting in lost profits for firms implementing the standard. As a result of these costs, patentees that may have faced meaningful competition prior to adoption of the standard may face little competition after the fact. Hold-up occurs when a patentee uses these switching costs to demand higher royalty rates than it could have negotiated before the standard was adopted.

Where a firm acquires market power through deception or other exclusionary conduct, patent hold-up can be an antitrust violation, as the Commission maintained in its Dell, $^4Unocal^5$ and $Rambus^6$ cases. And, as the Commission concluded in N-Data, 7 conduct that permits patent hold-up can violate Section 5 of the FTC Act even if it does not necessarily violate Section 2 of the Sherman Act.

³ Patent hold-up is a specific example of opportunism that can arise in the face of sunk costs, a problem that is well recognized in the economic literature. See U.S. DEPT. OF JUSTICE & FED. T

However, even where patent hold-up does not raise an antitrust enforcement issue, it remains an important issue for competition policy more broadly. The risk of hold-up distorts the alignment between investment and reward, and

least two SSOs VITA and IEEE several years ago adopted patent policies that encourage firms holding essential patents to disclose the most restrictive licensing terms they would demand, including maximum royalty rates. Because most SSOs prohibit discussion of royalty rates as part of the standard setting process due to antitrust risks, both organizations asked the Department of Justice to review their proposed policies prior to adoption. In both instances, the Justice Department evaluated the policies under the rule of reason and concluded that it had no intention of challenging the policies.
Following letters, some expected similar policies to proliferate across SSOs. Yet, it is my understanding that VITA and IEEE are the only major SSOs that permit consideration of royalty rates as part of the standard setting process, which raises another interesting set of issues

negotiations may lead to royalties that reflect the collective bargaining power of the licensees, rather than the value of the technology exclusive of switching costs.¹¹

In our joint Intellectual Property Report in 2007, the Commission and the Justice Department stated that joint negotiation policies will be evaluated under the rule of reason, 12 which raises interesting and difficult questions regarding the standards for defining the relevant market, and proving market power and competitive effects. 13 At least one commentator has argu

look first at whether joint negotiations are reasonably necessary to support the procompetitive benefits of the collaboration.¹⁴ I would be interested to learn more from our panelists today about whether in fact joint negotiation policies are likely to offer practical advantages over other tools to limit patent hold-up.

After lunch, our third panel will discuss RAND royalty commitments—the imiting patent hold-up. Many SSO rules require members to commit to license patents to those practicing the standard on reasonable and nondiscriminatory terms. While some believe that the RAND commitment works adequately to clarify licensing terms and frees SSO members to focus on technical merit

rather than royalty rates, others claim that a RAND commitment is too vague to provide meaningful protection against patent hold-up.¹⁵

In our recent report on the Evolving IP Marketplace, the Commission recommends that damages for infringement of a patent subject to a RAND commitment should reflect the outcome of a hypothetical negotiation between a willing licensee and licensor at the time the standard was set. In this hypothetical negotiation, a licensor will not be able to charge more for its technology than the value it provides to a licensee over the next best alternative at the time the infringer invested in the technology. Properly applied, the hypothetical negotiation framework aligns reward with contribution by linking royalty awards to the market value of a technology. But some claim the approach risks harming incentives to innovate or is too difficult to implement. Our third panel will address both the theoretical and practical issues associated with this and other approaches to clarifying the RAND commitment.

Let me conclude by thanking the panelists once again for participating today and sharing their knowledge and various perspectives. I think we can all look forward to a lively and interesting discussion of these important issues. Thank you.

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¹⁵ See, e.g., Gilbert, supra note 13 (arguing that reasonable royalties are inherently ambiguous and calling for greater attention to the nondiscriminatory prong of the RAND commitment as a way to limit patent hold-up).

¹⁶ THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION (March 2011), at 191-94, available at