Patent Misuse After Princo Corp. v. Int'l Trade Commission

On August 30, 2010, the Court of Appeals for the Federal Circuit issued an *en banc* decision in *Princo Corporation v. International Trade Commission* affirming the International Trade Commission's ("ITC") ruling that the U.S. Philips Corporation ("Philips") was not precluded by patent misuse from asserting its patents against Princo Corporation ("Princo").[1] The decision effectively limits the scope of the patent misuse doctrine and may have implications in the licensing efforts of joint ventures.

Background

Philips and the Sony Corporation ("Sony") worked together to develop standards for the technology associated with recordable compact discs ("CD-Rs") and rewritable compact discs ("CD-RWs"). Those standards were collected in a publication entitled "Recordable CD Standard," which is more commonly known as the "Orange Book."

During the development process, both Philips and Sony found different solutions to the problem of encoding position information on the disc.[2] Phil-ips' solution was described in the Raaymakers patents, two of the patents at issue in this case. Sony's approach was set forth in the Lagadec patent, which was *not* asserted against Princo.

For purposes of the Orange Book standard, Philips and Sony agreed to adopt the approach described in the Raaymakers patents. Philips and Sony engineers found that approach to be "'simple and … work[] very well.'" In contrast, the solution described in the Lagadec patent was thought to be "'prone to error'" and "'very difficult'" to implement.[3]

To commercialize their technology, Philips and Sony offered various package licenses for the patents required to manufacture CDR/RW discs per the Orange Book standard. Included in the package licenses were both the Raaymakers and Lagadec patents. The licenses included a field of use provision that limited use of the patents to manufacturing Orange Book-compliant discs.

Despite entering into a license agreement with Philips in the late 1990s, Princo stopped paying the required licensing fees. This prompted Philips to file a complaint with the ITC alleging that Princo was importing infringing CD-Rs and CD-RWs.

Raising patent misuse as an affirmative defense, Princo argued that "Philips had improperly forced Princo and other licensees, as a condition of licensing patents that were necessary to manufacture CD-Rs or CD-RWs, to take licenses to other patents that were not necessary to manufacture those products."[4] Princo's patent misuse defense was based upon an alleged agreement between Philips and Sony to "suppress" the Lagadec technology (and not separately license the Lagadec patent), essentially to the benefit of the Raaymakers patents.

Although the administrative law judge at the ITC found Philips' patents were infringed, the judge denied relief to Philips on the basis that the patents were unenforceable due to patent misuse. That ruling, of course, was not the final word on the issue. Since that ruling, the case has taken an extensive path, with an appeal of the ITC's ruling to the Federal Circuit, a remand, another ruling by the ITC followed by a second appeal to the Federal Circuit, and culminating in an *en banc* hearing before the Federal Circuit and the subject opinion.

No Leveraging, No Patent Misuse

In considering whether patent misuse was present in this case, the Federal Circuit reviewed Supreme Court precedent and the basic rule established by that precedent—"the patentee may exploit his patent but may not 'use it to acquire a monopoly not embraced in the patent.'"[5] The majority opinion emphasized that, in view of the broad scope of licensing conditions that a patentee may impose, "the doctrine of patent misuse 'has largely been confined to a handful of specific practices by which the patentee seemed to be trying to "extend" his patent grant beyond its statutory limits.'"[6] The majority noted that the scope of patent misuse was narrow, and is not available to an infringer simply because the patentee engages in wrongful commercial conduct that might have anticompetitive effects.[7] "While proof of an antitrust violation shows that the patentee has committed wrongful conduct having anticompetitive effects, that does not establish misuse of the patent in suit unless the conduct in question restricts the use of that patent and does so in one of the specific ways that have been held to be outside the otherwise broad scope of the patent grant."[8]

The majority opinion reduced the issue to its simplest form—"[w]hen a patentee offers to license a patent, does the patentee misuse that patent by inducing a third party not to license its separate, competitive technology?"[9] For patent misuse to exist, reasoned the majority, there must be connection between the patent right and the misconduct at issue.[10] The Court found no connection between the alleged agreement between Philips and Sony to suppress the availability of the Lagadec technology and the asserted patents, the Raaymakers patents. The possibility of an antitrust violation with respect to the Lagadec patent did not make Philips liable for misuse of the Raaymakers patents.[11]

Specifically, the agreement did not "leverage the power of a patent to exact concessions from a licensee that are not fairly within the ambit of the patent right."[12] In the *Princo* case, unlike in the *Morton Salt* case,[13] the Raaymakers patents were not used to restrain competition with the patentee's sale of an unpatented product. The majority concluded that this was not a case where conditions had been placed on licenses that went beyond the physical or temporal scope of the patent grant, and accordingly held that there was no patent misuse.[14] "What patent misuse is about, in short, is 'patent leverage,' i.e., the use of the patent power to impose overbroad conditions on the use of the patent in suit that are 'not within the reach of the monopoly granted by the Government.'"[15]

No Anticompetitive Effect, No Patent Misuse

Having concluded that there was no patent misuse on the first basis, the majority opinion continued the analysis and also found no patent misuse on a second, separate basis—Princo's failure to establish that the alleged agreement between Philips and Sony to "suppress" the Lagadec technology had anticompetitive effects. Despite Princo's urging to the contrary, the Court refused to overrule the line of the authority requiring a showing of anticompetitive effects for patent misuse.

Relying on the findings of the ITC, the majority found that the alleged agreement did not suppress a viable technology that could have competed with the Orange Book standard.[16] The ITC found that the Lagadec technology did not work well, was prone to errors, and was not a commercially or technically viable approach to that of the Raaymakers patents.[17] Further, the ITC noted that Princo failed to show that any potential licensee had considered developing the Lagadec technology to compete with the discs made according to the Orange Book.[18] In view of the evidence (or lack thereof), the majority found that Princo failed to establish that the alleged agreement had any market effect at all, let alone the necessary anticompetitive effects required under the rule of reason analysis, and thus concluded that there was no patent misuse.

The majority discussed at length the many benefits of joint ventures, noting that

> [c]ollaboration for the purpose of developing and commercializing new technology can result in economies of scale and integrations of complementary capacities that reduce costs, facilitate innovation, eliminate duplication of effort and assets, and share risks that no individual member would be willing to undertake alone, thereby "promot[ing] rather than hinder[ing] competition."[19]

The majority further highlighted that "cooperation by competitors in standard-setting 'can provide procompetitive benefits . . . '" such as greater product interoperability, positive network effects, and "incentives to innovate by establishing a technical baseline for further product improvements."[20] Clearly, all these benefits were considered by the Court in rendering its decision.

The Dissent

The 42-page majority slip opinion was accompanied by a sharply worded, 32-page dissent authored by Judge Dyk and joined by Judge Gajarsa. The dissent vigorously disagreed with the majority's conclusion that there was nopatent misuse. Rather, it viewed the alleged agreement between Philips and Sony to suppress the Lagadec technology as "part and parcel of the same course of conduct designed to protect the Raaymakers patents from competition from the alternative Lagadec technology."[21] The dissent would have placed the burden on Philips to show that the agreement between Philips and Sony had legitimate justifications or lacked an anticompetitive effect.[22] The differences between the majority and the dissent in this decision are exemplified in the final paragraph of the dissent:

> The majority's strict standard fails to provide adequate protection against the suppression of nascent technology, and allows patent holders free rein to prevent the development of potentially competitive technologies except in the most extreme and unlikely circumstances.[23]

Practical Implications

The Court's attention to joint ventures and other collaborative efforts among competitors could be viewed as encouraging to their existence. This "encouragement" should not, however, be taken as a suggestion that joint ventures are free to impose any provision in any resulting patent pools without regard to patent misuse. While the majority highlighted the broad scope of protection provided to patentees in licensing their patents, collaborative ventures still need to avoid licensing practices that involve improper leveraging of patents and result in anticompetitive effects.

In view of the *en banc* decision, it will now be more difficult to establish a patent misuse defense. Not only will the accused infringer have to establish that the conduct involves "improper leveraging," it will also have to show that the conduct has an anticompetitive effect that stems from an asserted patent (or patents), not just in some general sense. This will be particularly challenging where the technology was not developed, perhaps due to an agreement to suppress that technology in the first place. Rather than relying on the doctrine of patent misuse, such parties may consider asserting antitrust counterclaims as those claims apply to a broader range of conduct, *i.e.*, not limited to the asserted patent.

In sum, this decision represents a narrowing of the patent misuse doctrine and will likely give patentees greater latitude to enter into more creative collaborative venture agreements, pushing the boundaries of what is considered anticompetitive behavior.

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Endnotes

1. 616 F.3d 1318 (Fed. Cir. 2010).
2. *Id.* at 1322.
3. *Id.*
4. *Id.* at 1323.
5. *Id.* at 1327.
6. *Id.* at 1329.
7. *Id.*
8. *Id.*
9. *Id.* at 1331.
10. *Id.*
11. *Id.* at 1332.
12. *Id.* at 1333.
13. *Morton Salt Co. v. G.S. Suppiger Co.*, 314 U.S. 488 (1942).
14. *Id.* at 1331.
15. *Id.*
16. *Id.* at 1336-37.
17. *Id.* at 1337.
18. *Id.* at 1338.
19. *Id.* at 1335 (quoting DOJ and FTC, *Antitrust Guidelines for the Licensing of Intellectual Property*, §§ 5.1 at 24 and 5.5 at 28, Apr. 6, 1995).
20. *Id.* at 1335.
21. *Id.* at 1346.
22. *Id.* at 1354.
23. *Id.* at 1357.