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Managing Antitrust Risks in Patent Licensing – Post-Expiration Royalties and Package Licensing

By Paul A. Ragusa and Guy Eddon[1]

Patent owners have considerable freedom to negotiate the subject matter, price, and term in licensing agreements. However, antitrust law has been used to limit this freedom when an arrangement is considered to exceed the statutory patent rights and produce anticompetitive effects. Consequently, it has been considered "black letter law" for fifty years that a patent owner cannot attempt to obtain royalties in a pure patent license after all licensed patents have expired, and certain tying arrangements in patent or other agreements have long been frowned upon.

Recent developments in this area are challenging both doctrines. Can a patent owner charge royalties even after patent expiration, in instances where a separate statutory scheme provides a licensable right? Although a royalty step-down at patent expiration is good practice, it may no longer be required in all cases. Can a patent owner engage in package licensing for wanted and perhaps unwanted patents, for example, a group of standard-essential and nonessential patents? These and other issues are addressed below.

<u>When is Post Patent Expiration Not an Antitrust Concern?</u>

A patent holder may not collect royalty payments beyond a patent's expiration date. *Brulotte v. Thys*, 379 U.S. 29, 32 (1964) (holding that "a patentee's use of a royalty agreement that projects beyond the expiration date of the patent is unlawful per se."). The rule is founded in the idea that a patent holder should not be permitted to use a license "to project its monopoly beyond the patent period," thereby subjecting "the free market visualized for the post-expiration period ... to monopoly influences that have no proper place there." *Id.* at 32–33. While a few cases have criticized its reasoning, *Brulotte* has remained the law for fifty years. *See, e.g., Zila, Inc. v. Tinnell*, 502 F.3d 1014, 1019 n. 4 (9th Cir. 2007); *see also Scheiber v. Dolby Labs.*, *Inc.*, 293 F.3d 1014, 1017 (7th Cir. 2002).

Recently, however, one district court distinguished the *Brulotte* rule from statutory schemes that provide for market exclusivity not based on a patent's expiration date. *See Astrazeneca AB v. Apotex Corp.*, 01-cv-9351, 2013 WL 6244425 at *31 (S.D.N.Y. Dec. 3, 2013). The "pediatric exclusivity period" provides a six-month period during which time the FDA is barred from approving an Abbreviated New Drug Application ("ANDA") for a generic drug that infringes another's patent. Food and Drug Administration Modernization Act of 1997, 21 U.S.C. § 355a(b)(1)(B)(ii). The practical effect of the statute is to bar the sale of a generic during the six-month pediatric exclusivity period. *See Janssen Pharmaceutica, N.V. v. Apotex, Inc.*, 540 F.3d 1353, 1362 n. 7 (Fed. Cir. 2008).

In *Astrazeneca*, the defendant argued that, under *Brulotte*, it "would be impermissible to include royalty payments for the pediatric exclusivity period in any damages calculation, because a patent holder may not collect royalty payments beyond a patent's expiration date." *Astrazeneca*, 2013 WL 6244425 at *31. However, the district court found that payments made during the six-month period were not impermissible royalty payments on an expired patent but, rather, in a hypothetical negotiation, could be viewed as

[1] Mr. Ragusa is a partner and Mr. Eddon an associate in the New York office of Baker Botts, LLP, where they practice intellectual property law including patent litigation, licensing, and counseling.

payments made to induce the plaintiff to waive its additional six-month period of market exclusivity created by statute. *Id.* at 32.

Federal Circuit law supports the view that market exclusivity is permissible even after an underlying patent has expired. *In re Omeprazole Patent Litig.*, 536 F.3d 1361 (Fed. Cir. 2008). In that appeal, the Federal Circuit rejected the argument that "the district court may not grant relief relating to the period of market exclusivity after a patent has expired," holding instead that the district court could "provide a post-expiration remedy for infringement under section 271(e)(2)." *Id.* at 1367-68.

It is still generally good practice to include a royalty step down at the time the last patent expires, particularly since the Supreme Court has yet to consider the carve out discussed above that may be developing in the courts. While some courts may be willing to characterize "royalties" paid after patent expiration as "waiver" payments made in consideration of the expired patent holder's live exclusivity right, certain judges and juries might nevertheless find that waiver of a statutory right after the expiration of an underlying patent is worth somewhat less than the license fee while the patent is still in force. The defendant in the *Astrazeneca* case made that exact argument, in part because after expiration of the plaintiff's patent, it was no longer an infringement to make the drug—the defendant was only restricted from selling it for six months, which is significantly less protection than the full bundle of property rights enjoyed by a patentee.

Packaging Licensing Agreements for Standard Essential Patents

"Many tying arrangements, even those involving patents and requirements ties, are fully consistent with a free, competitive market." *Illinois Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 45 (2006). In particular, "it is not an unlawful tying arrangement for a seller to include several items in a single mandatory package when the items may be reasonably considered to constitute parts of a single distinct product." *Int'l Mfg. Co. v. Landon, Inc.*, 336 F.2d 723, 730 (9th Cir. 1964). Improper tying arrangements, by definition, involve two separate products. *Id.*

An important factor when determining whether a group of patents cover a single article is whether the proposed package license includes blocking patents necessary for that article. *Id.* Antitrust concerns can arise in mandatory package licensing when "the prospective licensee, in order to obtain a license under one patent, would be compelled to accept licenses under patents that were not necessarily needed." *Id.* at 729. Where multiple blocking patents cover a single article, however, the "licensee is being compelled to accept no more than he would, in any event, have to obtain in order to make worthwhile a license under any of the patents." *Id.* at 730.

The question of permissible package licensing is further complicated by the presence of Standard Essential Patents ("SEPs"), which can be voluntarily declared by their owner to be essential to the practice of a standard (*e.g.*, Wi-Fi or 3G.). A patent that is essential to practice a standard can enable the patent holder to exclude others from making products compatible with that standard. For this reason, many Standard-Setting organizations ("SSOs") have adopted rules and requirements for the licensing of SEPs, and generally require that SEPs be licensed on Fair, Reasonable, and Nondiscriminatory ("FRAND") terms.

Applying the reasoning of *Landon*, mandatory package licensing is permissible for SEPs, so long as the tied SEPs are required to practice one standard. Since the patents are all part of the standard, they may be considered blocking patents for producing a product compatible with that standard. Package licensing overcomes the problem inherent in "licensing patent rights on a patent-by-patent basis," which "can result in continuing disputes over whether the licensee's technology infringes certain ancillary patents owned by the licensor that are not part of the group elected by the licensee." *U.S. Philips Corp., v. Int'l Trade Comm'n*, 424 F.3d 1179, 1198 (Fed. Cir. 2005).

There are also circumstances where a patent holder may wish to package nonessential patents with SEPs. Packaging SEPs with related nonessential patents does not give rise to an antitrust violation or otherwise constitute misuse *per se*. *Id.* at 1187-88 (distinguishing the *per se* rule of patent misuse when tying patented goods with non-patented goods from the tying of essential and nonessential patents in a license agreement); *Koninklijke Philips N.V. v. Cinram Int'l, Inc.*, 08-cv-0515, 2013 WL 2301955 at *4 (S.D.N.Y. May 24, 2013), appeal dismissed (Sept. 18, 2013).

The Federal Circuit has stated that patents "can be regarded as 'nonessential' only if there are 'commercially feasible' alternatives to those patents." *Id.* at 1194, citing *Landon*, 336 F.2d at 729. Where there are no commercially feasible alternatives to allegedly nonessential patents, "packaging those patents together with so-called essential patents can have no anticompetitive effect in the marketplace, because no competition for a viable alternative product is foreclosed." *Id.* Moreover, "a package licensing agreement that includes both essential and nonessential patents does not impose any requirement on the licensee." *Id.* at 1190. In so holding, the court explicitly rejected the Commission's ruling that package agreements constitute *per se* patent misuse. *Id.* at 1197.

Another issue that can arise involves so-called "ancillary restraints," such as agreements between collaborators not to compete against their joint venture. Such agreements are assessed under the rule of reason. *Princo Corp. v. Int'l Trade Comm'n*, 616 F.3d 1318, 1336 (Fed. Cir. 2010) (*en banc*). In *Princo,* the Federal Circuit, sitting *en banc*, held that an agreement to refrain from licensing a patent for use outside a standard is not presumptively anticompetitive. *Id*. Treating the standard-setting process and patent pool as a joint venture, and a standard as an ancillary restraint, the court held that the patent holders "acted legitimately in choosing not to compete against their own joint venture." *Id.* at 1334.

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Although once set in stone, recent case law is providing patent owners with greater flexibility to structure license agreements. In some circumstances, patent owners may be able to charge royalties even after the applicable patents expire. Patent owners may likewise be able to engage in package licensing and embed ancillary restraints in their license agreements under certain reasonable circumstances.