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Antitrust Rulemaking as a Solution to Abuse on the Standard-Setting Process

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NOTE

ANTITRUST RULEMAKING AS A SOLUTION TO ABUSE OF THE STANDARD-SETTING PROCESS

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While many recognize the critical role that technology plays in modern life, few appreciate the role that standards play in contributing to its success. Devices as prevalent as the modern laptop computer, for example, may be governed by over 500 interoperability standards, regulating everything from the USB drive to the memory chip. To facilitate adoption of such standards, firms are increasingly turning to standard-setting organizations. These organizations consist of members of an industry who agree to abide by the organization's bylaws, which typically regard topics such as patent disclosure and reasonable licensing. Problems arise, however, when members violate these bylaws after a standard has been adopted. Where a member asserts its patents against other members in violation of the organization's bylaws, that member engages in what is known as "patent holdup." Both private and public litigation have focused on curbing this practice, but the current regime remains imperfect. This Note argues that the best approach to the current problem of patent holdup requires the Federal Trade Commission to promulgate an antitrust rule. This approach combines the advantages associated with traditional enforcement with the beneficial aspects of agency rulemaking.

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INTRODUCTION

Some technological advancements provide benefits by themselves. However, the vast majority of devices available to the consumer are in reality aggregations of independent patented technologies that are packaged together and that rely on interoperability standards to function.[1] The personal computer is a prominent example of this concept.[2] Personal computers combine various technologies, such as DVD drives, USB outlets, and memory chips, which each rely on interoperability among products to be fully functional. If there were twenty different standards for DVDs that required twenty different players, consumers would experience dramatically fewer benefits. Thus, it is important that industry settle on standards for interoperability among products.

There are two primary ways in which an industry can settle on a standard: through the regular course of competition, which often gives rise to "standard wars," or through standard-setting organizations ("SSOs").[3] Standard wars, such as the recent Blu-ray/HD DVD conflict and its predecessor the VHS/Betamax conflict, rely on the marketplace to decide which standard prevails.[4] This process can be long, and it leads consumers either to purchase the losing standard or wait for the market to decide on a standard.[5] To avoid these problems, industries can convene SSOs.[6] SSOs are groups composed of members of a certain industry, such as the memory chip indus-

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1. *See* Christopher Hardee, *Single-Firm Opportunism and the FTC's* Rambus *Defeat: Implications for Section 2 of the Sherman Act*, 18 TEX. INTELL. PROP. L.J. 97, 98–99 (2009).

2. It is estimated that over 500 different interoperability standards are required to produce a typical laptop computer. Brad Biddle et al., *How Many Standards in a Laptop? (And Other Empirical Questions)*, PROC. 2010 ITU-T KALEIDOSCOPE ACAD. CONF. 123, 125, *available at* http://www.itu.int/dms_pub/itu-t/opb/proc/T-PROC-KALEI-2010-PDF-E.pdf.

3. *See* Patrick D. Curran, Comment, *Standard-Setting Organizations: Patents, Price Fixing, and Per Se Legality*, 70 U. CHI. L. REV. 983, 988–92 (2003).

4. *See* S.J. Liebowitz & Stephen E. Margolis, *Should Technology Choice Be a Concern of Antitrust Policy?*, 9 HARV. J.L. & TECH. 283, 290–95, 314–16 (1996); David J. Teece & Edward F. Sherry, *Standards Setting and Antitrust*, 87 MINN. L. REV. 1913, 1915 (2003); Curran, *supra* note 3, at 989 n.26.

5. *See* Hardee, *supra* note 1, at 99; Liebowitz & Margolis, *supra* note 4, at 293–94.

6. *See* Mark A. Lemley, *Intellectual Property Rights and Standard-Setting Organizations*, 90 CALIF. L. REV. 1889, 1896–98 (2002) (discussing the need for standard-setting in the face of complex technology demands).

try, who meet to decide on industry standards.[7] Because the members set standards as a group, consumers benefit from interoperability among their products and are not forced to decide which standard to adopt.[8] Further, industry benefits from increased and accelerated consumer adoption of its standard.[9]

While SSOs provide many benefits to consumers and industry, some members of SSOs have devised ways to abuse the standard-setting process in order to extract greater returns. Through a practice known as "patent holdup," patent holders of a technology that will become a standard wait until their technology has been adopted by the SSO, and then "hold up" the manufacturing process by charging higher royalties to extract greater profits from the manufacturers.[10] Patent holdup harms consumers not only by increasing the price of technology[11] but also by delaying the standard-setting process and erasing the efficiency gains that attract industry to SSOs in the first place.[12]

In order to combat these abusive practices, both the government and private parties have brought actions against SSO members who use patent holdup tactics, but the current state of the law has failed to establish sufficient disincentives to prevent these tactics for good. Reliance on private parties and the Sherman Act has proven ill suited for this new wave of anticompetitive practice. In response, the Federal Trade Commission ("FTC" or "the Commission") has invoked section 5 ("Section 5") of the Federal Trade Commission Act ("FTCA"), which declares unlawful "[u]nfair methods of competition," to combat these abuses.[13] This approach, while somewhat effective, remains an incomplete solution due to concerns arising from the expansion of the provision's application to a point at which it begins to harm industry participants and elicit judicial and congressional backlash.[14] There is, however, an alternative approach. By adopting a *rule* under the "unfair methods of competition" prong of the FTCA, the FTC can benefit from the

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7. *Id.* at 1892–93.

8. *See* Hardee, *supra* note 1, at 98–99, 99 n.6.

9. *See id.*

10. Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 310 (3d Cir. 2007); *see also* Bruce H. Kobayashi & Joshua D. Wright, *Federalism, Substantive Preemption, and Limits on Antitrust: An Application to Patent Holdup*, 5 J. COMPETITION L. & ECON. 469, 489 (2009) (discussing cases where deception was used to extract royalties through patent holdup).

11. *See* Mark A. Lemley & Carl Shapiro, *Patent Holdup and Royalty Stacking*, 85 TEX. L. REV. 1991, 2011–17 (2007) (explaining through modeling that patent holdup results in higher prices and lower output).

12. *See id.* at 2016 (explaining how injunctions or threats of injunctions hold up manufacture of products relying on a standard).

13. 15 U.S.C. § 45(a)(1) (2006).

14. *See* Workshop on Section 5 of the FTC Act as a Competition Statute 4–20 (Oct. 17, 2008) [hereinafter Section 5 Workshop], *available at* http://www.ftc.gov/bc/workshops/section5/transcript.pdf (opening remarks of William Kovacic, Chairman, Fed. Trade Comm'n) (explaining reluctance on the part of the Commission to bring actions under an independent Section 5).

independence and flexibility of Section 5, give greater notice to industry of what practices will be unlawful, and assure the courts that this new application of Section 5 will not lead to limitless expansion of the provision.

This Note argues that the FTC should use its antitrust rulemaking authority to promulgate a rule that declares it a violation of Section 5 of the FTCA for firms to engage in deception and other anticompetitive conduct in abuse of the standard-setting process. Part I explains the problem of patent holdup and reveals how reliance on private action and the Sherman Act's monopolization provision is insufficient to combat it. This insufficiency is due to inherent limitations in the antitrust statute and contract law. Part II discusses the benefits and drawbacks of an "independent"[15] Section 5 in the standard-setting context and argues that Section 5, while an improvement over Sherman Act and contract litigation, still presents an incomplete solution to patent holdup. Finally, Part III advocates promulgation of an antitrust rule by the FTC that draws on the benefits of Section 5 while providing clear boundaries that should alleviate industries' and courts' major concerns.

I. CHALLENGING PATENT HOLDUP IN STANDARD-SETTING ORGANIZATIONS

The problem of patent holdup cannot be solved by reliance on SSOs, private actions, or the Sherman Act. Section I.A looks at the abuses that have developed to take advantage of the standard-setting process and explains how these abuses result in anticompetitive consequences that require legal action. Section I.B surveys the efforts that SSOs and private parties take to combat these abuses and explains how these efforts face inherent limitations that make reliance on them insufficient. Section I.C examines the Sherman Act's application in the standard-setting context and discusses how limitations both in the underlying statute and in legal precedent make the Sherman Act a tool ill suited to combating abuse in SSOs.

A. *The Problem of Patent Holdup*

SSOs are groups, often composed of competitors within an industry, that meet over a period of time to develop an industry standard.[16] During the standard-setting process, the group evaluates members' contributions (pa-

15. "Independent" Section 5 refers to the FTC's use of this provision without reference to the Sherman Act. As discussed *infra* in Section II.A, the FTC may not directly enforce the Sherman Act, but rather must use Section 5 of the FTCA with a reference to the Sherman Act. Where the FTC desires to use Section 5 beyond the limits of the Sherman Act, it invokes Section 5 without reference. This is known as an enforcement action under an independent Section 5. *See* Daniel A. Crane, *Reflections on Section 5 of the FTC Act and the FTC's Case Against Intel*, 2010 COMPETITION POL'Y INT'L ANTITRUST CHRON. 1, 3–5 [hereinafter Crane, *Reflections on Section 5*].

16. Lemley, *supra* note 6, at 1892–93.

tented technologies) on their technical and practical merits.[17] SSOs may adopt either an "open" or a "closed" standard as a result of this process.[18] Open standards are those that "are not controlled by any one party and can be adopted freely by all market participants."[19] Closed standards involve one or more specific patented technologies that require royalty licensing.[20] In choosing whether to adopt an open or closed standard, the SSO may weigh the competing interests and incentives of members to decide on a standard that meets the needs of the industry and that manufacturers feel confident integrating into their products.[21]

This process, however, has a major flaw. While it is capable of producing a number of procompetitive results, it is also open to abuse by its members through patent holdup, which may have a detrimental impact on competition and consumers. Patent holdup may take a variety of forms and may affect both open and closed standards.[22] For example, a member of an SSO may fail to disclose its patent during the standard-setting process and may either remain silent or encourage the group to adopt its technology as a standard without the other members knowing the implications of their decision. Once the SSO adopts the technology and expends a substantial amount of time and money integrating the standard into new and existing products, the patent holder may make known its ownership of the patent and bring patent infringement actions against users of the standard.[23] On the opposite end of the spectrum, a patent holder may make its patents known to the SSO and promise licensing at a nominal rate. Once the patent is integrated into the final standard, however, the patent holder may use its newly obtained market power to extract substantial royalties from the other members.[24] While these are just two examples of possibilities for abuse, there are countless variations on the general principle that they represent: patent holders can easily abuse the standard-setting process for their own gain.

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17. Joseph Scott Miller, *Standard Setting, Patents, and Access Lock-In: RAND Licensing and the Theory of the Firm*, 40 IND. L. REV. 351, 365 (2007).

18. Lemley, *supra* note 6, at 1901–02.

19. Curran, *supra* note 3, at 990; *see also* Lemley, *supra* note 6, at 1902.

20. *See* Lemley, *supra* note 6, at 1901–02.

21. *See id.*

22. *See* Robert A. Skitol & Kenneth M. Vorrasi, *Patent Holdup in Standards Development: Life After* Rambus v. FTC, ANTITRUST, Summer 2009, at 26, 28 (discussing how recent precedent permits scenarios where patent holdup may occur in both the "open" and "closed" standard context); *see also* Section 5 Workshop, *supra* note 14, at 240–43 (remarks of Robert A. Skitol, Partner, Drinker, Biddle & Reath LLP) (offering a series of hypothetical scenarios giving rise to patent holdup).

23. *See, e.g.*, Rambus Inc. v. FTC, 522 F.3d 456, 460–61 (D.C. Cir. 2008) (discussing the lag between standard adoption and patent disclosure).

24. *See, e.g.*, Negotiated Data Solutions LLC, File No. 051-0094, 2008 WL 258308, at *5 para. 37(a) (F.T.C. Jan. 22, 2008) (charging that the defendant anticompetitively increased its royalty rates).

Patent holdup is harmful for a variety of reasons. First, patent holdup delays the implementation of a standard.[25] One of the reasons for forming an SSO is to accelerate the adoption of new standards;[26] so, in delaying the process, patent holdup directly undercuts the aim of the entire system. Second, by taking advantage of their enhanced market position, patent holders also harm competition by reducing output, increasing costs to manufacturers, and excluding manufacturers.[27] Each of these methods is likely to result in increased costs to consumers.[28] Third, patent holdup discourages participation in SSOs and harms innovation.[29] Where the danger of abuse undermines the collaborative process by threatening to extract supracompetitive prices from competitors, industry members are less likely to participate in SSOs in the future and, as a result, consumers are less likely to benefit from these organizations.[30] And fourth, the costs of patent holdup inflicted on industry members, both in litigation and in royalty payments, draw funding away from research and development and, in extreme cases, may drive some companies out of business.[31] Given the harmful consequences patent holdup may have on consumers and the marketplace as a whole, the question quickly turns to what can be done to stop it.

B. *Deficiencies in Private Action*

While there is a range of legal options available to private parties injured by patent holdup, sounding in areas from contract to tort law, private action alone cannot provide a complete solution to the problem.[32] One reason for this is the way SSOs operate. Through their bylaws, SSOs ensure that each member agrees to a series of requirements in order to take part in the standard-setting process.[33] These requirements typically include agreements to disclose patents and to license these patents on reasonable and nondiscriminatory ("RAND") terms.[34] However, the terms of these agreements are

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25. *See* Gil Ohana et al., *Disclosure and Negotiation of Licensing Terms Prior to Adoption of Industry Standards: Preventing Another Patent Ambush?*, 24 EUR. COMPETITION L. REV. 644, 644–45 (2003).

26. *Cf.* Teece & Sherry, *supra* note 4, at 1914–17 (discussing benefits of adoption of a standard in the context of the alternative "standards war").

27. *See generally* Lemley & Shapiro, *supra* note 11, at 2010–17 (discussing the harm to victims of patent holdup).

28. *See id.* at 2013.

29. *Id.* at 1993.

30. *Id.*; *see* Section 5 Workshop, *supra* note 14, at 228–31 (remarks of Scott Peterson, Senior Counsel, Hewlett-Packard Co.).

31. *See* Lemley & Shapiro, *supra* note 11, at 1992–94.

32. *See generally* Lemley, *supra* note 6, at 1909–37 (discussing legal avenues available to private parties and the failings of this enforcement mechanism).

33. *Id.* at 1904.

34. *See id.* at 1902–04, 1973 (providing a survey of SSO agreements); Mark A. Lemley, *Ten Things To Do About Patent Holdup of Standards (And One* Not *To)*, 48 B.C. L. REV. 149, 156 (2007).

intentionally left vague to avoid potential antitrust liability. If the terms of the SSO agreement are too specific—for example, listing pricing requirements for patented technologies—they could be viewed as illegal price-fixing agreements.[35] As a result, SSO bylaws often provide at most a questionable foundation on which to base litigation over patent licensing disagreements.[36]

Moreover, many firms—particularly third-party beneficiaries—are unable to pursue action through traditional legal routes. In the SSO context, third-party beneficiaries are industry members who have chosen not to participate in the SSO. Once the SSO selects a standard, these firms are still exposed to both the benefits of the standard-setting process and the problems that arise from patent holdup. But while members of the SSO may have weak claims against a firm engaged in patent holdup, third-party beneficiaries were not even parties to the SSO agreement. They are therefore even more unlikely to bring any successful suit in instances of patent holdup.[37]

Even assuming that SSO members are willing and able to engage in litigation with a firm attempting patent holdup, consumer welfare takes a backseat to the members' financial considerations.[38] Because the incentives of the SSO members do not align with those of consumers, enforcement actions by firms in the private sector cannot be relied on to adequately protect consumers.[39] This concept is illustrated by a practice known as injunction threats, in which a patent holder threatens to bring an injunction against a manufacturer for violating its patent unless the manufacturer pays a substantial royalty.[40] While the patent holder's threat may have questionable

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35. Michael G. Cowie & Joseph P. Lavelle, *Patents Covering Industry Standards: The Risks to Enforceability Due to Conduct Before Standard-Setting Organizations*, 30 AIPLA Q.J. 95, 102 (2002) ("SSOs have been reluctant to specify or become involved in setting royalty rates for patented technology for fear that they will be accused of price fixing or another violation of the antitrust laws."); Amy A. Marasco & Elizabeth Dodson, *Invention and Innovation: Protecting Intellectual Property in Standard-Setting*, 2 INT'L J. IT STANDARDS & STANDARDIZATION RES. 49, 50 (2004).

36. *See* Cowie & Lavelle, *supra* note 35, at 144–45 (discussing a case in which the court found SSO bylaws too vague to support defendant's claims); *see also* Lemley, *supra* note 6, at 1964–67 (describing problems that arise from using an SSO term like "reasonableness" to defend against patent holdup).

37. *See* Lemley, *supra* note 6, at 1915–17 (explaining the limitations on third-party beneficiary claims against parties who engage in patent holdup); *see also* Request for Investigation of Rembrandt, Inc. for Anticompetitive Conduct That Threatens Digital Television Conversion from Albert A. Foer, President, Am. Antitrust Inst., to Donald Clark, Sec'y, Fed. Trade Comm'n (Mar. 26, 2008), *available at* http://www.ftc.gov/os/aai.pdf (requesting FTC action, in communication by third-party beneficiary, where firm repudiated RAND commitment to third party by claiming that actions related to an SSO did not create a contractual or other right as to third-party beneficiaries).

38. *See* Lemley & Shapiro, *supra* note 11, at 2008–17 (describing litigation-settlement decision by firms based on internal cost considerations).

39. *See* Section 5 Workshop, *supra* note 14, at 262–63 (remarks of Michael Lindsay, Partner, Dorsey & Whitney LLP) (discussing the incentives of manufacturers when faced with patent holdup).

40. Lemley & Shapiro, *supra* note 11, at 1992–94.

legal footing, the manufacturer will often pay the royalty instead of engaging in extended litigation.[41] This happens for several reasons. First, the manufacturer has a disincentive to engage a patent holder in litigation because the manufacturer will bear the cost of the litigation, the result of which could benefit competitors.[42] Companies will tend to pay the royalty and wait for another company to challenge the practice.[43] Second, the costs associated with challenging injunction threats may be substantial.[44] On top of ordinary litigation costs, if the manufacturer has already begun making and distributing goods based on the patented technology, a potential preliminary injunction could have a devastating effect on its business.[45] While engaging a patent holder in litigation may collaterally benefit consumers in that increased royalties are not passed through to the price of the ultimate product, this benefit does not tip the scales in favor of manufacturers pursuing such a path.[46] Thus, reliance on litigation by SSO members or other third parties will not provide a complete solution to patent holdup, as these parties serve as poor proxies for consumers.

C. *Deficiencies in the Sherman Act*

There are, however, other legal avenues that do take account of consumers' interests. The Sherman Act was adopted in 1890 in reaction to the power and wealth increasingly aggregated in large trusts.[47] The Act consists of two primary provisions: section 1 ("Section 1"), which prohibits combinations or conspiracies in restraint of trade,[48] and section 2 ("Section 2"), which prohibits monopolization of any part of trade or commerce.[49] In practice, Section 2 of the Sherman Act prevents anticompetitive and exclusionary conduct by single competitors, and thus is most applicable to the single-firm conduct at issue in the standard-setting context.[50] But application of this section is also subject to shortcomings.

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41. *See* Mark A. Lemley & Philip J. Weiser, *Should Property or Liability Rules Govern Information?*, 85 TEX. L. REV. 783, 786–88 (2007).

42. Section 5 Workshop, *supra* note 14, at 262–63 (remarks of Michael Lindsay, Partner, Dorsey & Whitney LLP).

43. *Id.*

44. *See* Lemley & Shapiro, *supra* note 11, at 2009; Lemley & Weiser, *supra* note 41, at 786–87; Section 5 Workshop, *supra* note 14, at 266–67 (remarks of Robert A. Skitol, Partner, Drinker, Biddle & Reath LLP).

45. Lemley & Shapiro, *supra* note 11, at 1992–93.

46. *See id.* at 1994–2010 (explaining that production concerns associated with an injunction drive firms to settle questionable infringement suits).

47. *See* David Millon, *The Sherman Act and the Balance of Power*, 61 S. CAL. L. REV. 1219, 1220–21 (1988).

48. 15 U.S.C. § 1 (2006).

49. *Id.* § 2.

50. *See* Gregory J. Werden, *Competition, Consumer Welfare, & the Sherman Act*, 9 SEDONA CONF. J. 87, 89–90 (2008).

Section 2 was instituted to prevent abuses of monopoly power, but abusive conduct in SSOs does not always fit neatly within monopolization theory.[51] Monopolization theory depends on conduct constituting "the willful acquisition or maintenance" of monopoly power "as distinguished from growth or development as a consequence of a superior product, business acumen, or historical accident."[52] It is difficult to apply this standard to the standard-setting context because the requisite traditional form of conduct, measured by whether a company has unlawfully acquired or maintained monopoly power (e.g., driving rivals out of business followed by monopoly pricing), is not present in that context.[53] SSOs involve collaboration among competitors; it is the collaborative efforts of the group that elevate the patent holder's patent to a level at which abuse of monopoly power may occur.[54] Because this collaboration is what grants the patent holder its power, abusive conduct in SSOs does not fit as neatly within Section 2 as traditional monopolization cases, and may as a result be substantially harder to contest in litigation under the antitrust statute.[55]

Not only do the Sherman Act's underlying statutory provisions make its use in the standard-setting context difficult, but judicial decisions have established Sherman Act precedent that requires increasingly more stringent tests, thereby making litigation under the Act an undesirable option.[56] This strict approach to the Sherman Act adopted by the courts is primarily due to the profound impact Section 2 cases have as precedent.[57] First, violations of the Sherman Act can carry substantial consequences. Those who violate the Act are subject to potential criminal penalties.[58] Also, where a court has found that a company has harmed competitors, that company is subject to treble damages (three times the amount of monetary harm inflicted on competitors).[59] Further, private actors may bring allegations of Sherman Act

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51. Herbert Hovenkamp, *The Federal Trade Commission and the Sherman Act*, 62 FLA. L. REV. 871, 874 (2010).

52. United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

53. Hardee, *supra* note 1, at 106–07 (explaining the problems of using Section 2 to combat standard-setting abuse and discussing how, even though it has been employed in cases such as *Rambus Inc. v. FTC*, 522 F.3d 456 (D.C. Cir. 2008), the statute lacks firm case law supporting its use against many forms of patent holdup).

54. Section 5 Workshop, *supra* note 14, at 228–31 (remarks of Scott Peterson, Senior Counsel, Hewlett-Packard Co.).

55. *See id.*; Hardee, *supra* note 1, at 107–08 (2009).

56. *See* Crane, *Reflections on Section 5*, *supra* note 15, at 3–5; *see also* Section 5 Workshop, *supra* note 14, at 72–80 (remarks of Daniel A. Crane, Professor, Benjamin N. Cardozo Sch. of Law).

57. *See* Crane, *Reflections on Section 5*, *supra* note 15, at 3–5.

58. 15 U.S.C. § 3 (2006) (establishing violation of the Sherman Act as a felony punishable by imprisonment and financial penalties); *id.* § 6 (allowing for forfeitures of property in transit); *id.* § 8 (establishing violations of the Sherman Act related to importation of goods as misdemeanor offenses).

59. *Id.* § 15 ("[A]ny person who shall be injured in his business or property . . . shall recover threefold the damages by him sustained.").

violations, magnifying the implications of judicial decisions.[60] Because of the impact these decisions could have on future cases, courts have increasingly sought to limit the Sherman Act's application by imposing more difficult standards on Sherman Act plaintiffs.[61]

One prominent example of the difficulty of bringing cases under the Act is *Rambus, Inc. v. FTC*.[62] As explained in greater detail in Part II,[63] *Rambus* involved an SSO organized to adopt a standard for memory chips.[64] During the standard-setting process, Rambus failed to fully disclose its patents to the organization.[65] After the group adopted a standard, based in part on patented technology owned by Rambus, Rambus brought royalty actions against memory chip manufacturers.[66] The FTC brought suit against Rambus under a monopolization theory based on Section 2 of the Sherman Act, arguing that, but for Rambus's failure to disclose its patent, the SSO would not have adopted its patent as its standard and Rambus would not have obtained its market power.[67] However, because the FTC was unable to prove with adequate certainty that Rambus's patent would not have been adopted had it properly disclosed its patents, the FTC failed to meet the Sherman Act's causation requirement, and judgment was returned for Rambus.[68]

With these weaknesses in the structure of the Sherman Act itself, and with the baggage it carries from recent precedent, the Act is not the ideal option for pursuing abuses in SSOs. Pursuing recourse through private action similarly fails to remedy the situation due to underlying deficiencies in courses of action available to the private sector.[69] A better solution to the problem must involve government action to take account of losses in general consumer welfare. However, that government action needs to be brought under a statute that is both flexible and unburdened by the baggage that comes with the Sherman Act. Section 5 of the FTCA satisfies both of these elements.

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60. Section 5 Workshop, *supra* note 14, at 254–55 (remarks of Jonathan Leibowitz, Comm'r, Fed. Trade Comm'n).

61. *Id.* at 211.

62. 522 F.3d 456 (D.C. Cir. 2008).

63. *See infra* Section II.C.

64. Specifically, the complaint pertained to Rambus's conduct regarding dynamic random access memory ("DRAM") technology. Complaint ¶ 1, Rambus Inc., File No. 011-0017, Docket No. 9302, 2002 WL 1436415 (F.T.C. June 18, 2002) [hereinafter Rambus Complaint].

65. *Id.* ¶¶ 54–55.

66. *Id.* ¶ 45.

67. *Rambus*, 522 F.3d at 462–67 ("In this case under § 5 of the FTC Act, the Commission expressly limited its theory of liability to Rambus's unlawful monopolization of four markets in violation of § 2 of the Sherman Act . . . . Therefore, we apply principles of antitrust law developed under the Sherman Act . . . .").

68. *Id.* at 463–64.

69. *See supra* Section I.B.

II. EMPLOYING SECTION 5 IN THE STANDARD-SETTING CONTEXT

Bringing suit under Section 5 of the FTCA solves many of the problems associated with private action and reliance on the Sherman Act, but it remains an incomplete solution to patent holdup. Section II.A of this Note establishes, through statute and precedent, the flexibility and independence of Section 5. Section II.B argues that those qualities remedy many of the deficiencies of enforcement in private actions and Sherman Act suits. Section II.C tracks the FTC's Section 5 enforcement actions in the standard-setting context, which demonstrate the benefits of enforcement under the section. Finally, Section II.D, drawing on these actions, contends that reservations related to the flexibility of Section 5 on the part of the Commission, the courts, and industry mean that reliance on enforcement actions brought under this provision is at best an incomplete solution.

A. *The Scope of Section 5*

The text and legislative history of Section 5 of the FTCA support the view that the provision would be a flexible tool to combat anticompetitive abuses, though subsequent judicial decisions have sometimes challenged the extent of the FTC's authority under the Act. The FTC was established in 1914 as an independent expert agency in the field of antitrust law with authority deriving from its enabling statute, the FTCA.[70] Section 5 of the FTCA, in vague terms, declares unlawful "[u]nfair methods of competition . . . and unfair or deceptive acts or practices in or affecting commerce."[71] When Congress passed the FTCA, it deliberately left these terms broad and undefined.[72] At the time, antitrust enforcement was within the jurisdiction of the Department of Justice under the Sherman Act.[73] The Sherman Act, while an effective litigation tool against practices that fell clearly within Sections 1 and 2, was not as effective against other anticompetitive practices.[74] Congress created the FTC to enforce Section 5 as a more flexible standard, prohibiting incipient violations.[75] In this way, Section 5 was not just coextensive with the

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70. Federal Trade Commission Act, 15 U.S.C. §§ 41–58 (2006); *see* Marc Winerman, *The Origins of the FTC: Concentration, Cooperation, Control, and Competition*, 71 ANTITRUST L.J. 1, 2, 75, 90–92 (2003) (describing the founding of the FTC).

71. Federal Trade Commission Act § 5(a)(1), 15 U.S.C. § 45(a)(1).

72. S. REP. NO. 63-597, at 13 (1914) ("[T]here were too many unfair practices to define, and after writing 20 of them into law it would be quite possible to invent others."); Neil W. Averitt, *The Meaning of "Unfair Methods of Competition" in Section 5 of the Federal Trade Commission Act*, 21 B.C. L. REV. 227, 228 (1980).

73. Averitt, *supra* note 72, at 230.

74. S. REP. NO. 62-1326, at 12 (1913) ("[A]s the statute is now construed there are . . . many other practices that seriously interfere with competition, and are plainly opposed to the public welfare, concerning which it is impossible to predict with any certainty whether they will be held to be due or undue restraints of trade.").

75. FTC v. Motion Picture Adver. Serv. Co., 344 U.S. 392, 394–95 (1953) (It is . . . clear that the Federal Trade Commission Act was designed to supplement and bolster the Sherman Act and the Clayton Act—to stop in their incipiency acts and practices which, when

Sherman Act but expanded the federal antitrust regime beyond the Sherman Act's reach.[76]

While the FTC appeared to have authority to bring action against any method of competition it deemed "unfair," in the Commission's early years it remained uncertain whether Section 5 mirrored Sections 1 and 2 of the Sherman Act or whether it could be employed to reach actions beyond the scope of the Act. This uncertainty was resolved in a series of Supreme Court decisions supporting a flexible interpretation of Section 5 independent of the Act.[77] In 1966, the Court in *FTC v. Brown Shoe Co.*[78] explained that the FTC, under Section 5, "arrest[s] trade restraints in their incipiency," and that this power "is particularly well established with regard to trade practices which conflict with the basic policies of the Sherman and Clayton Acts even though such practices may not actually violate these laws." This point was again stressed in the Court's 1972 decision in *FTC v. Sperry & Hutchinson Co.*[79] and in its 1986 decision in *FTC v. Indiana Federation of Dentists*,[80] in which the Court noted that Section 5 also covers "practices that the Commission determines are against public policy" in the antitrust context, grounds for action beyond those associated with the Sherman Act.

While the above cases demonstrate that the FTC has very broad authority in the antitrust arena, several appellate courts, particularly in *Official Airline Guides, Inc. v. FTC*,[81] *Boise Cascade Corp. v. FTC*,[82] and *E.I. du Pont de Nemours & Co. v. FTC*,[83] have suggested that this authority has limits. In the 1970s, the FTC brought these cases to expand the independent role of Section 5 in the antitrust context. But these efforts failed, and the resulting decisions continue to affect how the Commission approaches Section 5 cases.[84] While the decisions recognized that Section 5 allows the FTC to challenge behavior beyond the reach of the Sherman Act, they pushed

full blown, would violate those Acts, as well as to condemn as 'unfair methods of competition' existing violations of them." (citations omitted)); Averitt, *supra* note 72, at 242.

76. *See* FTC v. Sperry & Hutchinson Co., 405 U.S. 233, 244 (1972).

77. *E.g.*, *Motion Picture Adver.*, 344 U.S. at 394–95 ("The 'unfair methods of competition' which are condemned by Section 5(a) of the Act, are not confined to those that were illegal at common law or that were condemned by the Sherman Act."); *see also* Section 5 Workshop, *supra* note 14, at 64 (remarks of Robert Pitofsky, Sheehy Professor of Trade Regulation, Georgetown Univ. Law Ctr).

78. 384 U.S. 316, 321–22 (1966).

79. 405 U.S. at 242.

80. 476 U.S. 447, 454 (1986).

81. 630 F.2d 920 (2d Cir. 1980) (rejecting FTC's claim that a publisher of an airline schedule violated Section 5 by refusing to publish schedules for smaller airlines).

82. 637 F.2d 573 (9th Cir. 1980) (rejecting FTC's application of Section 5 against an independent parallel adoption of delivered pricing systems).

83. 729 F.2d 128 (2d Cir. 1984) (rejecting FTC's claim that the use of most favored nation clauses by two major suppliers was a violation of Section 5 because it facilitated parallel pricing).

84. *See, e.g.*, Complaint at *25–27, Negotiated Data Solutions LLC, File No. 051-0094, 2008 WL 258308 (F.T.C. Jan. 22, 2008) [hereinafter Negotiated Data Complaint] (Majoras, Comm'r, dissenting).

back on the FTC's interpretation of unfair conduct—a severe blow to the FTC's power.[85] Moreover, these decisions coincided with the Reagan Administration's minimalist approach to antitrust enforcement that limited FTC actions, cut FTC staff nearly in half, and statutorily restricted the FTC's jurisdiction.[86] This series of events has in many ways left the Commission shell-shocked, and serves as an ongoing roadblock to expanding Section 5.[87]

B. *Section 5 Remedies Deficiencies in the Current Enforcement Regime*

Section 5 is an important tool in fighting SSO abuse because it remedies several deficiencies apparent in a regime that otherwise depends on private action or Sherman Act enforcement. First, Section 5 provides an indirect remedy for SSO members and third-party beneficiaries. Under the current regime, third-party beneficiaries—firms that benefit from the standard-setting process but are not themselves members of the SSO—do not have as strong a cause of action as SSO members.[88] And even members' claims are weak, because the SSO agreements establish obligations so vague that they may not be sufficient bases for action.[89] Under an enforcement regime employing Section 5, however, the FTC could bring actions against SSO members who have abused the standard-setting process through patent holdup. This regime would not provide a new private cause of action, because only the FTC may enforce Section 5.[90] But it would allow the FTC to bring actions that might not otherwise be brought and to seek injunctive relief against firms engaged in patent holdup.[91] If not a complete solution to the problems faced by private parties, a regime under Section 5 could at least still solve many of those parties' concerns.

Second, unlike private litigation, enforcement actions under Section 5 would recognize consumer welfare considerations. In bringing these actions, the FTC considers the harm suffered by the firm but focuses primarily on

85. William E. Kovacic & Marc Winerman, *Competition Policy and the Application of Section 5 of the Federal Trade Commission Act*, 76 ANTITRUST L.J. 929, 942 (2010) ("In each instance, the court found that the Commission had failed to make a compelling case for condemning the conduct in question.").

86. William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 71 ANTITRUST L.J. 377, 384–86 (2003). *See generally* William E. Kovacic, *Public Choice and the Public Interest: Federal Trade Commission Antitrust Enforcement During the Reagan Administration*, 33 ANTITRUST BULL. 467 (1988) (discussing the shift in FTC enforcement priorities brought about by the Reagan Administration).

87. Crane, *Reflections on Section 5*, *supra* note 15, at 3–4; *see also* Section 5 Workshop, *supra* note 14, at 4–20 (remarks of William Kovacic, Chairman, Fed. Trade Comm'n).

88. *See supra* Section I.B.

89. *See supra* Section I.B.

90. *See, e.g.*, Holloway v. Bristol-Myers Corp., 485 F.2d 986, 988, 997 (D.C. Cir. 1973).

91. *See infra* Section II.C.

broader consumer welfare concerns associated with patent holdup.[92] This accords with the widely held view that the purpose of antitrust law—and thus antitrust enforcement actions—is to improve consumer welfare and prevent commercial activities that may harm consumers.[93] Because the FTC has an interest in maximizing consumer welfare, an enforcement regime under Section 5 offers benefits to consumers that alternative regimes cannot.

Finally, an enforcement regime under Section 5 would not be subject to the baggage carried by the Sherman Act. While private litigation has cabined the legal force of the Sherman Act, courts have not treated the FTCA in the same way.[94] The FTC faces no heightened legal burdens in asserting a scope of Section 5 that goes beyond the bounds of the Sherman Act—in fact, Supreme Court precedent supports such a construction.[95] Section 5 suits are thus more likely to succeed and to yield benefits to both consumers and industry.

C. *A History of FTC Actions in the Standard-Setting Context*

Through four major cases, the FTC has attempted to combat abuse of the standard-setting process. Together, these cases demonstrate that, while the FTC's current approach has been somewhat successful, it still remains an incomplete solution to the problem of patent holdup.

The FTC's first case against an SSO member for abuse of the standard-setting process was *Dell Computer Corp.*[96] In 1992, Dell became a member of the Video Electronics Standard Association ("VESA"), an SSO composed of virtually all major U.S. computer hardware and software manufacturers, and soon began actively participating in VESA's efforts to establish a standard for a computer bus design.[97] Once the group settled on a standard, Dell certified in writing that the standard did not infringe on any of its patents.[98] However, one year prior to the agreement, Dell had patented a technology that had been incorporated into the new standard, and after the bus design moved into widespread use, Dell announced to manufacturers that the design infringed on its patent and demanded appropriate compensation.[99] The FTC found that Dell had engaged in an unfair method of competition through patent holdup and entered an order preventing Dell from enforcing its patent.[100] A majority of the Commission stressed the importance of Section 5

92. *See, e.g.*, Dell Computer Corp., 121 F.T.C. 616, 626 (1996); *see also* Hovenkamp, *supra* note 51, at 878–79.

93. *See, e.g.*, *Dell*, 121 F.T.C. at 626; *see also* Thomas F. Cotter, *Patent Holdup, Patent Remedies, and Antitrust Responses*, 34 J. CORP. L. 1151, 1199 (2009).

94. *See* Crane, *Reflections on Section 5*, *supra* note 15, at 3–5.

95. *See supra* Section II.A.

96. 121 F.T.C. 616.

97. *Id.* at 617. A computer bus is a component of a computer that carries information internally. *Id.*

98. *Id.*

99. *Id.* at 617–18.

100. *Id.* at 618–22.

actions where consumer harm is likely, alluding to the fact that private parties fail to take consumers' interests into account in bringing actions in those situations.[101] The majority also added that, unlike other antitrust statutes, Section 5 "is particularly appropriate in this type of case, in which the legal and economic theories are somewhat novel."[102]

Next, in 2003, the FTC brought a complaint against Union Oil Co. ("Unocal").[103] The FTC alleged that the company had engaged in an unfair method of competition in violation of Section 5 by inducing the California Air Resources Board ("CARB") to adopt Unocal's patented technology.[104] CARB is a state body empowered to conduct standard-setting proceedings related to low-emission gasoline standards.[105] Unocal actively participated in certain CARB proceedings and, according to the complaint, made misrepresentations and engaged in other bad faith and deceptive conduct, creating the impression that it did not possess or would not enforce any relevant intellectual property rights.[106] It was only after refineries had spent billions of dollars adopting the resulting standard that Unocal commenced patent enforcement efforts.[107] In 2005, Unocal agreed to a consent order commanding it not to enforce these patents as a condition of its proposed merger with Chevron.[108]

In 2002, the FTC issued a complaint against Rambus, Inc. alleging, inter alia, that the company had engaged in a pattern of anticompetitive acts and practices over the preceding decade to monopolize a segment of the memory chip market, and that this conduct constituted an unfair method of competition under Section 5 of the FTCA.[109] Rambus's scheme arose from its participation in the Joint Electron Devices Engineering Council ("JEDEC"), an SSO convened to develop a memory chip standard.[110] Rambus had several patents that involved specific technologies proposed for, and ultimately adopted in, this standard.[111] In violation of JEDEC's bylaws, Rambus had concealed these patents through bad faith and deceptive conduct.[112] Once JEDEC's standard became widely adopted by the memory chip industry, Rambus began enforcing its patents, holding up the production process in

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101. *Id.* at 626.

102. *Id.*

103. Complaint ¶¶ 1–2, Union Oil Co. of Cal., File No. 011-0214, Docket No. 9305, 2003 WL 1190102 (F.T.C. Mar. 4, 2003).

104. *Id.*

105. *Id.* ¶ 1.

106. *Id.* ¶¶ 1–3.

107. *Id.* ¶¶ 5–6.

108. Union Oil Co. of Cal., Docket No. 9305, 2005 WL 2003365, at *3 (F.T.C. Aug. 2, 2005).

109. Rambus Complaint, *supra* note 64, ¶ 1.

110. *Id.* ¶ 2.

111. *Id.*

112. *Id.*

order to extract payments from manufacturers.[113] Rambus lost its case before the FTC, but appealed that decision to the U.S. Court of Appeals for the D.C. Circuit. In its argument before the D.C. Circuit, the FTC dropped its independent Section 5 claim and instead relied solely on a monopolization theory based on Section 2 of the Sherman Act.[114] Because Sherman Act precedent had established a strict causation standard, the FTC was unable to meet its burden, and the court entered judgment for Rambus.[115]

Finally, in 2008, the FTC issued a complaint against Negotiated Data Solutions LLC ("N-Data") alleging that the company had violated Section 5 by engaging both in unfair methods of competition and in unfair acts and practices, a separate prong of Section 5 that focuses more on consumer protection.[116] These alleged violations arose from N-Data's conduct related to the Institute of Electrical and Electronics Engineers ("IEEE"), an SSO involved in developing a computer networking standard.[117] Whereas the FTC's prior actions in the SSO context had been brought against firms for failing to disclose patents, this case involved N-Data's failure to license its patents on terms it had promised prior to the standard's adoption.[118] Not long after the complaint was issued, N-Data and the FTC entered into a consent agreement whereby N-Data agreed to cease enforcement of the relevant patents.[119]

These cases demonstrate a few important points. Most encouragingly, they show that the FTC is committed to bringing enforcement actions against standard-setting abuse and willing to aggressively pursue such abuse using novel theories, such as the introduction of the consumer protection prong of Section 5 in *N-Data*.[120] Less encouragingly, they also highlight the shortcomings of Section 5 enforcement.

One such shortcoming is the reluctance of some members of the FTC to expand the use of Section 5, which may undercut its effectiveness as a litigation tool. In some cases, this reluctance only appeared in the form of dissents. In *Dell*, for example, Commissioner Azcuenaga objected to the Commission's decision because the FTC's application of the statute seemed to lack clearly defined limits, potentially resulting in a "chilling effect" on

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113. *Id.* ¶ 2.

114. Rambus Inc. v. FTC, 522 F.3d 456, 467 (D.C. Cir. 2008) (describing the FTC's shift from Section 5 in the original complaint to a theory based entirely on the Sherman Act).

115. *Id.* at 462–67; *see also supra* notes 62–68 and accompanying text.

116. Negotiated Data Complaint, *supra* note 84, ¶ 1, at *1.

117. *Id.*

118. *Id.* ¶¶ 26–32, at *4–5. A different company had originally offered the contested royalty, but the claim carried to N-Data as successor to that company. *Id.* ¶¶ 12–13, at *2; *id.* ¶¶ 23–24, at *4.

119. Negotiated Data Solutions LLC, File No. 051-0094, Docket No. C-4234, 2008 WL 4407246, at *6–22 (F.T.C. Sept. 22, 2008).

120. Negotiated Data Complaint, *supra* note 84, ¶ 1, at *1; *see also* Robert P. Taylor, *Standard Setting: Where Are We After* Rambus *and* N-Data, *in* 15TH ANNUAL INSTITUTE ON INTELLECTUAL PROPERTY LAW 167, 176–79 (Practising Law Inst. ed. 2009) (noting the aggressive shift in enforcement against SSO abuse highlighted in the N-Data case).

participation in SSOs.[121] Chairman Majoras and Commissioner Kovacic echoed these concerns more recently in *N-Data*.[122] In *Rambus*, however, reluctance on the part of the FTC to rely on a novel use of Section 5 over a more traditional Sherman Act argument in the appellate court likely compromised the case itself.[123] The level of apprehension exhibited by the Commission in employing Section 5 in these cases is unlikely to diminish. Because of its potential to undermine future enforcement actions against patent holdup, this issue remains a serious concern.

Another issue that undermines the FTC's record of success in past Section 5 enforcement actions is the legitimacy of these actions. *Dell*, *Unocal*, and *N-Data* were resolved through settlement or adjudicative proceedings before the Commission,[124] and in *Rambus*, the FTC failed to present its Section 5 argument to the D.C. Circuit. Whether the provision may legitimately be used against patent holdup thus remains unresolved by an Article III court. This legitimacy issue stems from the concern that, while the Commission is ostensibly independent, it may be biased in favor of actions brought by the FTC.[125] For Section 5 to reliably combat patent holdup, the FTC would need to test its application through the appellate process in a federal court.[126]

D. *Remaining Problems with Section 5 Enforcement*

Issues of legitimacy and the commissioners' trepidation in the FTC's record of actions against standard-setting abuse suggest that an enforcement regime under Section 5 may not be the best solution to patent holdup. There are, however, other considerations outside of that record that tip the scales in favor of seeking an alternative means of combating patent holdup.

While Section 5's flexibility is beneficial in its gap-filling role, it also presents a problem. Whether a firm's conduct is "unfair" within the meaning of Section 5 is a subjective assessment on the part of the FTC. As such, industry is not always given sufficient notice of which actions are appropriate and which actions may result in antitrust scrutiny. Specifically, there is some fear that application of Section 5 to patent holdup may have a chilling effect

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121. Dell Computer Corp., 121 F.T.C. 616, 634–38 (1996) (Azcuenaga, Comm'r, dissenting).

122. Negotiated Data Complaint, *supra* note 84, at *23 (Kovacic, Comm'r, dissenting); *id.* at *27 (Majoras, Comm'r, dissenting).

123. *See* Rambus Inc. v. FTC, 522 F.3d 456, 467 (D.C. Cir. 2008) (noting the shift in the FTC's argument from Section 5 to the Sherman Act); *see also supra* text accompanying notes 109–115.

124. The FTC is a body of five commissioners appointed by the president. 15 U.S.C. § 41 (2006). The commissioners, in addition to voting to initiate enforcement actions and to take other agency action, may also serve as a panel in adjudicative proceedings on appeal from an administrative law judge. FTC decisions are appealable to a federal court of appeals. 16 C.F.R. pt. 3 (2010).

125. Rachel E. Barkow, *Institutional Design and the Policing of Prosecutors: Lessons from Administrative Law*, 61 STAN. L. REV. 869, 894–95 (2009).

126. *See* Kovacic & Winerman, *supra* note 85, at 941–42.

on SSO participation.[127] Much of the benefit of the SSO system derives from wide participation of industry members at many levels. This participatory process can produce procompetitive results that encourage innovation and benefit consumers through lower prices and efficient standard setting. In approaching potentially anticompetitive conduct by a firm, the FTC's use of Section 5 is generally bound by self-imposed limitations.[128] However, as *N-Data* illustrates, the FTC's perception of these limits, at least in the standard-setting context, is evolving. Where industry participants perceive an increased potential for liability arising from membership in SSOs, participation in SSOs will likely decline. And even where firms continue to participate, the process may grow to be so overcome by burdensome procedural safeguards as to eliminate many of the core benefits of collaborative standard setting that gave rise to the process to begin with. As the FTC continues to expand its use of Section 5 against patent holdup, concerns about the chilling effect that these actions may have on the standard-setting process become more salient and raise serious questions about the appropriate role of Section 5.

Another major concern with bringing cases under an independent Section 5 is that, as the application of the provision expands and the bounds of its flexibility are tested, the FTC risks eventual backlash from the courts or Congress similar to the backlash it experienced in the 1980s.[129] The FTC relies on Section 5 in both antitrust and consumer protection actions. A negative holding on Section 5's use in the standard-setting context may not only bear on future patent holdup enforcement efforts but may also severely impede the FTC's efforts in other areas. If the FTC fails to limit the application of Section 5, it risks subjecting Section 5 to the same or more severe judicial and congressional treatment than it experienced in the past.[130] Additionally, many states have their own statutes that are modeled after the FTCA. These state statutes are interdependent with the federal FTCA, and state courts interpret them using federal FTCA precedent.[131] Because holdings related to the FTCA at the federal level can, for better or for worse, impact these state statutes, unfavorable Section 5 precedent could also undermine actions at the state level.

The Commission's recognition of these risks may also pose a challenge to effective enforcement under Section 5 if fear of collateral effects chills enforcement actions that are genuinely warranted. The memory of the Commission's experience with Section 5 expansion from the 1970s and

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127. *See* Dell Computer Corp., 121 F.T.C. 616, 634–38 (1996) (Azcuenaga, Comm'r, dissenting).

128. Negotiated Data Complaint, *supra* note 84, at *25–26 (Majoras, Comm'r, dissenting); *see also supra* text accompanying notes 81–87.

129. *See supra* notes 81–90 and accompanying text; *see also infra* note 145.

130. *See supra* text accompanying notes 81–87; *see also infra* note 145.

131. *See* Negotiated Data Complaint, *supra* note 84, at *23–24 (Kovacic, Comm'r, dissenting).

1980s still lingers in the minds of commissioners and FTC staff,[132] and fears of collateral consequences continue to weigh on the FTC's actions today.[133] Thus, as new forms of anticompetitive conduct emerge, the FTC's reliance on Section 5 enforcement may be a poor legal avenue not only because of the potential backlash from Section 5 expansion but also because of the risk of inaction arising from the fear of potential collateral consequences.

III. ANTITRUST RULEMAKING AS A SOLUTION TO PATENT HOLDUP

By using its antitrust rulemaking authority, the FTC can rely on many of the benefits associated with Section 5 while avoiding the issue of unbounded authority that has evoked reservations on the part of industry, the courts, and members of the Commission. Section III.A explains the authority of the FTC to conduct antitrust rulemaking and argues that, while almost never used, such authority still remains a viable option open to the Commission. Section III.B discusses characteristics that an antitrust rule relevant to standard-setting abuse should have. Section III.C looks to potential concerns regarding enforcement by rule and balances those concerns against the benefits associated with adopting such a rule to remedy deficiencies in the standard-setting process.

A. *Authority for Antitrust Rulemaking*

Rulemaking is an attractive and sometimes necessary way in which administrative agencies carry out their responsibilities. Rulemaking authority is delegated to administrative agencies by statute, which establishes the bounds of that authority.[134] After an agency promulgates a rule according to procedures established under the Administrative Procedure Act ("APA"),[135] the rule becomes effective and the agency may, if the rule so specifies, enforce it in federal court.[136] Rules may also receive *Chevron* deference, a doctrine by which a court will defer to reasonable agency interpretations of ambiguous statutes that the agency administers.[137]

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132. *See supra* Section II.C.

133. *See, e.g.*, Negotiated Data Complaint, *supra* note 84, at *23–24 (Kovacic, Comm'r, dissenting) ("The Commission overlooks how the proposed settlement could affect the application of state statutes that are modeled on the FTC Act . . . .").

134. Steven P. Croley, *Theories of Regulation: Incorporating the Administrative Process*, 98 COLUM. L. REV. 1, 106–11 (1998).

135. 5 U.S.C. § 553 (2006).

136. *See id.* § 554. *See generally* Croley, *supra* note 134, at 106–11 (describing the rulemaking process).

137. Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842–45 (1984) (holding that courts should defer to an agency's reasonable interpretation when traditional methods of statutory interpretation render an ambiguous meaning); *see also* Thomas W. Merrill & Kristen E. Hickman, Chevron*'s Domain*, 89 GEO. L.J. 833, 833 (2001) (discussing *Chevron* deference).

Under section 6(g) of the FTCA, the FTC is authorized to promulgate rules with respect to "unfair methods of competition."[138] These rules have the force of law.[139] While the FTC has authority under this section to conduct antitrust rulemaking, it has almost never exercised it. The FTC has promulgated only one rule under this authority, and that rule was repealed after decades of disuse.[140] The FTC has considered other opportunities to promulgate antitrust rules, but none of those other efforts have ultimately produced a final rule.[141] Antitrust rulemaking in the standard-setting context may provide an excellent opportunity to revive this antitrust tool and fill a gap in the current enforcement regime.[142]

B. *Form of a Proposed Rule*

An antitrust rule might take any of a number of forms in order to effectively remedy the patent holdup problem. At one end of the spectrum, the FTC could promulgate a rule articulating specific licensing requirements. This could include not only specific disclosure obligations but also RAND or other pricing requirements. However, such a high degree of top-down control would place an impractical burden on the government and limit the flexibility that must be afforded to SSOs in crafting bylaws.[143] At the other end of the spectrum, the FTC could promulgate a rule in vague terms that mimic the ambiguities of Section 5. While this would allow for flexible enforcement, it would also give rise to serious concerns, including the argument that such a rule would undercut many of the advantages of the rulemaking process, such as effective notice to industry. A solution somewhere between these two points on the spectrum would likely yield the best results.

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138. Federal Trade Commission Act, 15 U.S.C. § 45 (2006); *see also* FED. TRADE COMM'N, OPERATING MANUAL ch. 7, § .4, at 33 (2003) [hereinafter FTC OPERATING MANUAL], *available at* http://www.ftc.gov/foia/ch07rulemaking.pdf ("[T]he Commission has statutory authority under FTCA § 6(g) to promulgate rules respecting unfair methods of competition.").

139. Nat'l Petroleum Refiners Ass'n v. FTC, 482 F.2d 672, 698 (D.C. Cir. 1973) (holding that the FTCA conferred broad powers on the FTC to make substantive rules and regulations); *see also* C. Scott Hemphill, *An Aggregate Approach to Antitrust: Using New Data and Rulemaking To Preserve Drug Competition*, 109 COLUM. L. REV. 629, 677 (2009).

140. *See* Discriminatory Practices in Men's and Boys' Tailored Clothing Industry, 59 Fed. Reg. 8527 (Feb. 23, 1994) (codified at 16 C.F.R. pt. 412) (repealing the previous rule governing promotional allowances in the mens' and boys' tailored clothing industry); Discriminatory Practices in Men's and Boys' Tailored Clothing Industry, 58 Fed. Reg. 35,907 (proposed July 2, 1993) (to be codified at 16 C.F.R. pt. 412) (issuing a notice of proposed rulemaking seeking comments on whether to repeal the rule).

141. *See, e.g.*, *FTC Staff Narrows Rulemaking Possibilities to Three Areas*, Antitrust & Trade Reg. Rep. (BNA) No. 884, at A-13 (Oct. 12, 1978) (noting potential antitrust rulemaking opportunities considered by FTC staff).

142. See *infra* Section III.C.1 for a more detailed discussion of the reasons behind the infrequent use of antitrust rulemaking.

143. *See infra* notes 148–151 and accompanying text.

An ideal rule would balance a preference for affording SSOs flexibility in setting internal rules—avoiding excessive top-down control—with the need for a rule specific enough to provide adequate notice to industry. This Note proposes one such formulation: a rule that declares failure of an original or successive patent holder to abide by an SSO rule or practice with respect to a member's patents or patent applications, or to adhere to any formal or informal commitment to the SSO with respect to the terms under which members may license its patents, to be an unfair method of competition within the meaning of Section 5. While this is a concise formulation, it contains several key elements that combat patent holdup.

First, the proposed rule is based on the "unfair methods of competition" prong of the FTCA. It is true that the consumer protection–focused "unfair acts and practices" prong of the Act might also be applicable in the SSO context, as demonstrated by its recent use in *N-Data*.[144] However, the procedural hurdles placed on that approach, more stringent than traditional APA procedures, make it a far less practical approach to take.[145] Unlike these burdensome procedures, antitrust rulemaking under the "unfair methods of competition" prong need follow only general APA rulemaking procedures.[146] As a result, potential rulemaking establishing an act as an "unfair method of competition" is a far more prudent approach.

Next, the proposed rule would ensure that the obligations it places on members of SSOs follow the underlying patents, so that the sale of a critical patent would not remove the rule's protections. This is an important element because of the FTC's lesson in *N-Data*: there, a licensing commitment was made by one company, but a successor company refused to honor it, insisting that it was not bound to license on the initial patent holder's promised terms.[147] By attaching obligations to the *patent* and not to the patent *holder*, fears of successor companies abandoning commitments on which SSO members rely in choosing a standard would diminish.

The proposed rule would also buttress SSOs' rules, rather than marking a shift to top-down government regulation of the standard-setting process. A top-down model would not only strip SSOs of their flexibility but would also require the government to shoulder the impossible task of setting SSO bylaws and licensing terms amenable across commercial sectors. Flexibility is critical for SSOs, which often arise in industries undergoing rapid technological change. Moreover, even where SSOs operate within the same general sector, each SSO is typically formed to address specific technologies that

144. Negotiated Data Complaint, *supra* note 84, ¶¶ 1–2, 38.

145. *See* Marc Winerman, *The FTC at Ninety: History Through Headlines*, 72 ANTITRUST L.J. 871, 890 (2005); *see also* H.R. REP. No. 11-367, pt. 1, at 104 (2009) ("Congress instituted the Magnuson-Moss rulemaking procedures in the 1970s due to its growing concern that the FTC, which at the time was carrying out multiple wide-ranging concurrent rulemakings, should be required to carry out more structured rulemaking procedures.").

146. 5 U.S.C. § 553 (2006); *see also* FTC OPERATING MANUAL, *supra* note 138, § .4 (discussing procedures for rulemaking under the unfair competition powers in Section 5).

147. *See supra* notes 116–119 and accompanying text.

require distinct solutions.[148] One size does not fit all.[149] Disclosure obligations that an SSO deems appropriate, for example, may vary depending on both the technology and external considerations, such as potential participants' reluctance to join the SSO due to overly burdensome disclosure rules.[150] Some standards may require royalty-free licensing; SSOs convened to set others may prefer RAND licensing, or set no specific licensing obligations for its members at all.[151] In such a complex climate, it is nearly impossible for the government to act as a top-down rulemaking and rate-setting organization, because it is hardly capable of analyzing industry conditions and establishing rules that will effectively promote rather than chill innovation in all cases.

Finally, the proposed rule would still be specific enough to provide some notice to industry. A major problem with traditional enforcement under Section 5 is that, because the provision is so flexible, market participants do not know whether their activities will be subject to FTC action. This creates a degree of unease that can have a chilling effect on innovation. The proposed formulation of this rule states that violations occur where members fail to adhere to commitments made to the SSO, or to SSO rules or practices related to patents or patent applications. While perhaps not an ideal solution from the perspective of patent holders, this text would provide clear notice that violating explicit SSO rules or procedures as to patents, or failing to adhere to other SSO-mandated commitments, would be construed as an unfair method of competition. It would similarly act as a default rule for SSOs and their members. SSOs, aware that antitrust authorities will only buttress existing rules rather than broaden them with expansive Section 5 enforcement, would renew their focus on articulating member obligations with sufficient clarity to merit protection as an "SSO rule or practice" within the meaning of the proposed rule. SSOs would also craft bylaws that make it clear that, in agreeing to them, members are making a "commitment" to the SSO within the meaning of the proposed rule.[152] Members, for their part, would likely show greater interest in ensuring that they are correctly interpreting obligations imposed on them by the SSO. This is because, where in the past patent holders could rely on weaknesses in private actions, SSO rules under this regime would be buttressed by the threat of FTC enforcement.

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148. *See* Workshop on Tools To Prevent Patent "Hold-Up" 38–41 (June 21, 2011) [hereinafter "Hold-Up" Workshop], *available at* http://www.ftc.gov/opp/workshops/standards/transcript.pdf (remarks of Earl Nied, Program Dir., Intel Corp.).

149. *See* Lemley , *supra* note 6, at 1904 (describing a survey conducted in which twenty-four of thirty-six SSOs analyzed imposed either an express or implied obligation that members disclose intellectual property rights of which they were aware).

150. *See* "Hold-Up" Workshop, *supra* note 148, at 47–51 (remarks of Amy Marasco, Manager, Microsoft Corp.).

151. *See id.*

152. Even though SSOs are limited by antitrust laws in that they are unable to require terms such as specific pricing, they may still address issues including patent disclosure and *reasonableness* of pricing. *See supra* notes 33–36 and accompanying text.

C. *Broad Considerations Associated with Enforcement by Rule*

The previous Section spoke to the specific elements of the proposed rule formulation. However, some general issues arise under a system driven by agency enforcement by rule rather than through traditional litigation. This Section addresses the concerns and benefits of the proposed enforcement approach.

1. Concerns with Enforcement by Rule

One concern is that enforcement by rule is essentially untested and may therefore be a poor outlet to rely on in situations of such profound impact as patent holdups. Opportunities for antitrust rulemaking have been discussed by a variety of legal scholars[153] and FTC staff.[154] While the FTC has promulgated one rule under its antitrust rulemaking authority,[155] the rule was made over forty years ago and has since been repealed because it was deemed unnecessary by FTC staff.[156] Some have questioned whether antitrust rulemaking is a practical solution to antitrust problems in light of the many unanswered questions that exist about how courts and others will react to FTC rules.[157]

This concern is not fatal to this Note's approach. The FTC has substantial experience promulgating and enforcing rules under the consumer protection prong of Section 5.[158] This suggests that the FTC should be experienced enough to translate its success under that half of Section 5 to the "unfair methods of competition" half, and demonstrates that courts are not unfamiliar with FTC rulemaking. Moreover, disuse of antitrust rulemaking authority is not a major problem. Rather, it simply suggests that traditional enforcement actions have in the past suited the needs of the FTC. As commerce evolves, however, the FTC should be able to tailor its enforcement solutions to the demands of the rapidly developing sectors that employ SSOs. Concerns as to a new application of the FTC's existing antitrust rulemaking authority to these sectors should not weigh too heavily against the use of such authority.

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153. *See, e.g.*, Daniel A. Crane, *Technocracy and Antitrust*, 86 TEX. L. REV. 1159, 1206–10 (2008) [hereinafter Crane, *Technocracy*].

154. *See, e.g.*, *FTC Staff Narrows Rulemaking Possibilities to Three Areas*, *supra* note 141, at A-13 (describing potential antitrust rulemaking opportunities considered by FTC staff).

155. Discriminatory Practices in Men's and Boys' Tailored Clothing Industry, 32 Fed. Reg. 15,584 (Nov. 9, 1967) (to be codified at 16 C.F.R. pt. 412) (issuing notice of a final rule).

156. Discriminatory Practices in Men's and Boys' Tailored Clothing Industry, 59 Fed. Reg. 8527 (Feb. 23, 1994) (codified at 16 C.F.R. pt. 412) (repealing the previous rule governing promotional allowances in the mens' and boys' tailored clothing industry).

157. *E.g.*, Crane, *Technocracy*, *supra* note 153, at 1206–10 (discussing how the success of antitrust rules turns on questions such as whether courts would view antitrust law as lending itself to a rule-based approach).

158. *Cf.* Federal Deposit Insurance Corporation Improvement Act of 1991 § 40(a)(1), 12 U.S.C. § 1831t (2006) (requiring the FTC to issue a rule prescribing the manner and content of certain disclosures and of enforcement of the rule).

Another concern regards the political implications of the FTC invoking its antitrust rulemaking authority. One of the benefits often cited by proponents of rulemaking is that the rulemaking process, through notice and comment procedures, often brings important topics to Congress's attention.[159] There is, however, a corresponding risk that Congress may grow concerned about the FTC's increasing intervention in the technology sector. In the 1970s and 1980s, the FTC experienced backlash from Congress due to its activism in the consumer protection arena.[160] As a result, the FTC's authority and resources were curtailed, and procedures for promulgating rules under the consumer protection prong of Section 5 became so burdensome that they rendered FTC-initiated consumer protection rulemaking an impractical and rarely used tool.[161] With an approach based on the "unfair methods of competition" prong, there may be a concern that FTC intervention in the technology sector could trigger a similar response from Congress.

This too is not fatal to the approach. The proposed rule uses a light touch in that it only buttresses rules established by SSOs. Because the rule would support actions by the private sector to manage their own activities rather than introducing additional agency oversight, Congress would be unlikely to react the way it did when the FTC's activism in the consumer protection arena evoked fears of excessive government intervention.

One final concern with the approach is that it will demand more of the FTC in a regulatory capacity than the FTC is capable of handling. For example, under any rule where the FTC would be called upon to enforce RAND terms, the FTC might fall into the role of license-rate regulator, determining which licensing fees are reasonable and which are unreasonable. But the FTC is a relatively small institution with limited resources.[162] Some are concerned that under such a scenario the Commission would have to bring on new staff with expertise in the technology sector to monitor the reasonableness of licensing terms arising from SSO commitments.[163]

This concern is unlikely to be serious under the proposed formulation. As to the problem of determining "reasonableness," the FTC has already developed expertise in this area and, in fact, recently authored a report putting forth workable solutions to the problem of calculating "reasonableness" in the context of RAND commitments.[164] Further, the FTC would not need to establish itself as a monitoring body and would not incur the related costs

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159. *See* Hemphill, *supra* note 139, at 680–81.

160. Winerman, *supra* note 145, at 890; *see also* Kovacic & Winerman, *supra* note 85, at 943 ("In the . . . 1970s, Commission efforts to use Section 5 litigation to reach beyond prevailing interpretations of Sections 1 and 2 of the Sherman Act elicited strong political backlash from the Congress.").

161. *See* H.R. REP. No. 11-367 (2009); *supra* notes 81–87 and accompanying text.

162. *See* M. Sean Royall et al., *Deterring "Patent Ambush" in Standard Setting: Lessons from* Rambus *and* Qualcomm, ANTITRUST, Summer 2009, at 34, 36–37.

163. *See* Crane, *Technocracy*, *supra* note 153, at 1205.

164. FED. TRADE COMM'N, THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION 21–25 (2011), *available at* http://www.ftc.gov/os/2011/03/110307patentreport.pdf.

of increases in staff and resources. Rather, enforcement of the proposed rule would operate similarly to the FTC's enforcement of its consumer protection rules. Under that regime, companies and individuals report fraudulent activity that violates one of the FTC's rules, which the Commission then investigates and, at its discretion, prosecutes.[165] Because the burden would be on the private sector to report in such a regime, the FTC would not need to monitor SSO activity. And as with consumer protection enforcement, a small number of decisive enforcement actions against abusive firms should act as a deterrent sufficient to decrease the FTC's litigation workload.[166] Thus, despite some legitimate concerns with the approach of enforcement by rule, those concerns are not fatal to the strategy. Moreover, the next Section demonstrates that there are also general benefits to enforcement by rule that weigh in favor of the approach.

2. Benefits of Enforcement by Rule

While there are some issues associated with choosing to combat patent holdup by rule, the benefits of selecting a rule-based approach generally outweigh those issues. One of the greatest benefits of adopting a rule is that it provides clear notice to industry. Section 5 is a broad provision; new cases that rely on an expanding interpretation of it have increasingly drawn concerns from industry, the courts, and members of the FTC.[167] The Act's flexibility has left those in the technology sector unclear about the scope of the statute and uncertain about whether specific patent holders' actions are subject to FTC enforcement or whether they are permissible. Under such a regime, manufacturers may become dissuaded from participating in SSOs out of concern that the law might not capture critical standard-setting abuses, and patent holders might be dissuaded from participating in SSOs out of fear of antitrust liability. But under a rule-based approach, industry has a better idea of the boundaries of the law. This should provide patent holders some disincentive from engaging in patent holdup and SSO members some assurance that good faith participation in SSOs will not lead to antitrust liability.

The rulemaking process also offers SSO members an opportunity to be involved in developing the FTC rule itself. APA procedures would require the FTC to use a notice-and-comment system of rulemaking, whereby the FTC must seek public comment on its proposed rule.[168] This gives SSOs and SSO members an opportunity to comment on the rule, offering suggestions

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165. FED. TRADE COMM'N, THE FTC IN 2011, at 21–50 (2011), *available at* http://www.ftc.gov/os/2011/04/2011ChairmansReport.pdf (discussing the FTC's annual activities in consumer protection).

166. *See, e.g.*, FED. TRADE COMM'N, GENERIC DRUG ENTRY PRIOR TO PATENT EXPIRATION (2002) (concluding that FTC investigations and enforcement deterred anticompetitive pharmaceutical agreements).

167. *See supra* Section II.C.

168. 5 U.S.C. § 553 (2006); *see also* FTC OPERATING MANUAL, *supra* note 138, § .4 (describing FTC rulemaking procedures); Croley, *supra* note 134, at 106–11.

about how the rule should be framed and presenting any concerns they may have with the FTC's formulation of it. The final rule would thus likely receive greater support from SSOs than an alternative regulation might otherwise receive, and it may be more effective as a result of comments submitted by industry insiders.

Another benefit of rulemaking is that it limits FTC enforcement in the standard-setting area, allaying concerns related to the seemingly limitless scope of Section 5. Such concerns have been raised not only by industry but by members of the Commission as well.[169] They are based on the fear that FTC actions under an ever-expanding Section 5 could result in backlash from the courts that could diminish the effectiveness of future enforcement actions.[170] In bringing patent holdup actions under a rule, the Commission may both alleviate this fear and initiate actions it might not otherwise bring due to worries about judicial reaction and other collateral effects. Moreover, by adopting an enforcement-by-rule approach, the FTC eases its burden at trial in that it need only show that a party violated the rule to prove its prima facie case. This simplified enforcement structure benefits industry and others concerned about expansive use of Section 5, and also benefits the FTC's enforcement efforts against SSO abuse by reducing its burden at trial.

Finally, the FTC, as an agency with expertise in antitrust law, is more capable of crafting a rule to remedy the patent holdup problem than the courts would be in a system that relied on the judiciary to set the tone of enforcement in the SSO context.[171] "Rulemaking yields higher-quality policy decisions than adjudication because it invites broad participation in the policymaking process by all affected entities and groups, and because it encourages the agency to focus on the broad effects of its policy rather than the often idiosyncratic adjudicative facts of a specific dispute."[172] In crafting a rule with the force of law, the FTC directly addresses the patent holdup problem in the context of a broader antitrust policy agenda. Relying on the courts to develop the law through precedent is an inexact method that may not provide a complete solution to the problems at hand. Courts generally have little antitrust expertise and thus may not be suitable outlets for setting effective antitrust policy.[173] The FTC, by contrast, is an agency of antitrust experts with decades of experience in the field. Its staff is acutely aware of the antitrust considerations at play in the standard-setting context and capable of promulgating a rule that speaks directly to those considerations while

169. *See, e.g.*, Negotiated Data Complaint, *supra* note 84, at *22–23 (Kovacic, Comm'r, dissenting).

170. *See supra* Section II.C.

171. *See* Hemphill, *supra* note 139, at 673–74.

172. Richard J. Pierce, Jr., *Two Problems in Administrative Law: Political Polarity on the District of Columbia Circuit and Judicial Deterrence of Agency Rulemaking*, 1988 DUKE L.J. 300, 308.

173. *See, e.g.*, Michael R. Baye & Joshua D. Wright, *Is Antitrust Too Complicated for Generalist Judges? The Impact of Economic Complexity and Judicial Training on Appeals*, 54 J.L. & ECON. 1 (2011) (concluding that antitrust cases are too complicated for generalist judges).

minimizing any negative collateral effects.[174] The problem of patent holdup is more likely to be remedied by vesting policymaking in the FTC through the rulemaking process than by relying solely on the courts.

CONCLUSION

With the increasingly important role technology plays in our lives, it is important that the law continue to foster an environment in which technological innovation can flourish. The adoption of the standard-setting mechanism by the technology sector seems to have outpaced the law: current legal protections have proven insufficient to prevent the abusive practice of patent holdup that appears in SSOs. Where patent holders are able to abuse the standard-setting process to the detriment of others in the industry, it not only harms consumers by driving prices higher but also threatens to inhibit technological advancement.

While looking to enforcement actions under Section 5 of the FTCA may appear to be an attractive alternative to more traditional reliance on contract law or the Sherman Act, it remains an incomplete solution. Instead of relying on an overly broad FTCA or an overly narrow Sherman Act, consumers and industry would be better served through the FTC rulemaking process. A rule that makes violations of SSO bylaws unlawful unfair methods of competition under the FTCA would carry the benefits of Section 5 without many of the drawbacks that litigation under that statute brings. The rule proposed in this Note would provide notice to industry and assurance to the courts regarding the bounds of FTC action, while remaining flexible enough to capture patent holders who might otherwise find a way to circumvent the law. Though not without its own difficulties, it is clear that a rule-based solution is well suited to remedy the current deficiencies in the law, and can thereby promote innovation and growth in the technology sector that will benefit both industry and consumers.

174. *See* Crane, *Technocracy*, *supra* note 153, at 1159–65, 1197–202 (describing the development of the FTC into an agency of antitrust experts and arguing that such expertise justifies expanding the FTC's norm-creation authority in antitrust); Pierce, Jr., *supra* note 172, at 308 (speaking to the preference to defer to administrative agencies and the rulemaking process to take advantage of the expertise of agency staff).