



DEPARTMENT OF JUSTICE

THE ROLE OF ANTITRUST IN INTELLECTUAL PROPERTY

Address by

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Today marks my first anniversary of being confirmed as Assistant Attorney General for Antitrust, and I am truly grateful to President Clinton and Attorney General Janet Reno for the opportunity to serve our nation.

I am delighted to have this opportunity to outline the Division's views on a vitally important issue: the intersection of antitrust enforcement and the protection of intellectual property rights. Today's topic, "Intellectual Property into the 21st Century," is especially appropriate and timely. It is appropriate because intellectual property is the engine for jobs and economic growth, now and in the future. It is timely because we have been actively evaluating our enforcement policy in the past few months and will soon issue new intellectual property Guidelines. In addition, just three weeks ago, we filed our first non-merger intellectual property case in fifteen years. What I hope to convey today is not only the guiding principles of our enforcement policy, but how intelligent antitrust enforcement can spur innovation.

At the outset, I wish to stress that antitrust is not a doctrinaire political field. It is law enforcement, and the people of this country expect and deserve that enforcement to be fair, even-handed and non-partisan. Our recent settlement of the airlines case illustrates the non-partisan nature of antitrust enforcement: it was the product of three successive Administrations' work. So also does the historic AT&T case, whose prosecution, settlement and consent decree enforcement activities now represent a monumental 20-year project of the Antitrust Division. I intend to build upon this tradition of fair, even-handed and non-partisan enforcement of antitrust law.

I start by observing that the Division -- and the Federal Circuit -- both share responsibility to ensure that our intellectual property system continues to be, as Abraham

Lincoln once stated, "the fuel of interest to the fire of genius." We do so in distinctly different roles -- ours in law enforcement against abusive intellectual property arrangements and yours in adjudicating intellectual property cases.

The creation of the Federal Circuit to adjudicate patent cases has brought much needed expertise to a highly technical field and has fostered a greater respect for intellectual property rights.

Lest there be any misunderstanding, I take this opportunity to restate our strong support for intellectual property rights -- they are vital to our economy and they protect the inventors and creators of intellectual property. The various intellectual property regimes reward innovation by giving rights to creators to exclude others from using their inventions or the expression of their ideas without compensation. If this were not the case, then others could "free ride" on the efforts of innovators. Without appropriate protection, the incentives to engage in costly innovation would be significantly reduced.

Strong intellectual property protection is especially important in the high tech industries that represent America's and the world's economic future. That is why the United States pushed so hard during the Uruguay Round, for example, to ensure that other countries extend to our nationals a similar degree of intellectual property protection to that found here.

In expressing my support for strong intellectual property rights, I am by no means suggesting that one should confer intellectual property rights where they are inappropriate. The awarding of patent-like protection in the absence of an adequate showing of novelty and non-obviousness, for example,

can harm competition without serving the interest of rewarding innovation. More important, inappropriate patent protection can stand in the way of subsequent innovation by blocking further developments, eliminating the incentives of subsequent innovators to engage in such innovation, and raising the costs and risks of R&D generally. For this reason, we support the efforts of the Patent and Trademark Office to reexamine questionable patents and to ensure that its examiners have the appropriate background, training, and databases to make correct decisions on patent applications in the first instance. In addition, in our role as the Administration's competition advocate, we support the DeConcini Bill's proposals to end so-called "submarine" patents and to provide a 20 year term from filing. These proposals seek, in our view, the proper balance between the use of an invention and the protection of efforts to invent. We will continue to work closely with Commissioner Bruce Lehman to ensure that patents are used appropriately and competitively.

I also believe that strong antitrust enforcement promotes the legitimate exercise of intellectual property rights. Strong intellectual property rights and vigorous antitrust enforcement are two sides of the same coin in promoting the common objective of innovation.

Indeed, the fallacy, commonly stated in some circles, that the intellectual property laws and the antitrust laws are inherently in conflict should be laid to rest. The Federal Circuit refuted this perception best in the case of Atari v. Nintendo: "[T]he aims and objectives of patent and antitrust laws may seem, at first glance, wholly at odds. However, the two bodies of law are actually complementary, as both are aimed at encouraging innovation, industry and competition."

Because innovation in our industries has been so important to competition and the U.S. economy, there is a long

history of Antitrust Division enforcement activities in the intellectual property area. During the 1960's and 1970's and up until 1985, the Division had a separate Intellectual Property Section. It was very active, filing 16 cases in 12 years. In 1985, however, the Intellectual Property Section was folded into the Professions Section, and by 1993, the Division had only two lawyers specializing in intellectual property.

When I first became Assistant Attorney General, leading members of the antitrust bar advised me that there was a need to refocus our enforcement activities in the intellectual property area. In particular, concern was raised that several foreign firms may have abused intellectual property rights to monopolize or attempt to monopolize industries important to U.S. exports. These practices were said to be causing U.S. companies to lose jobs and exports.

We moved quickly to address this issue. We hired additional lawyers with intellectual property backgrounds and opened a number of investigations. These efforts have borne fruit -- three weeks ago we filed a significant case in the float glass industry, which I will describe in a few minutes.

In addition, as I announced in January of this year at the celebration of the 60th Anniversary of the Antitrust Division, and as I reiterated in several speeches since then, we are revising the 1988 Antitrust Enforcement Guidelines for International Operations to reflect the Antitrust Division's current views of its enforcement intentions, and we are creating two new Guidelines to take its place, one for intellectual property and one for international-related issues. To formulate our new policy in intellectual property, I created a Division Task Force to write new Guidelines and to consult with experts from academia, industry, the bar, and the

Clinton Administration on intellectual property issues. We will publish proposed Intellectual Property Guidelines in the Federal Register for public comment in the next few weeks. I urge interested parties to comment on them when they are published in the Federal Register. We will seriously consider these comments before we adopt the Guidelines and they will certainly help us articulate a "real-world" view of what antitrust enforcement should entail.

If I had to summarize our enforcement policy, I would state as follows: "The Division strongly supports intellectual property rights. Those rights can provide important incentives to innovate. We will not, however, turn a blind eye toward abusive intellectual property arrangements that reduce incentives to innovate."

It is our belief that competition and innovation are inseparable. Our intellectual property enforcement policy is about keeping American companies strong and innovative. We realize that intellectual property provides the foundation for jobs and economic growth.

The correlation between competition and innovation is at the heart of Professor Michael Porter's recently acclaimed work, The Competitive Advantage of Nations. Observing that corporate managers often support lenient merger and collaboration policies because it is a "tempting way to raise short-term profits," Professor Porter views such policies as the path to national decline. Pointing to empirical evidence that "active domestic rivalry is strongly associated with international success," he concludes that "a strong antitrust policy, especially in the area of horizontal mergers, alliances and collusive behavior, is essential to the role of upgrading any economy." Id. at 663.

The lesson from Professor Porter's book is that innovation thrives in markets that are competitive. Indeed, many studies of national economies reveal that rivalry, not market power, fosters innovation and efficiency over the long run. For that reason, I have observed that antitrust enforcement promotes, rather than impedes, innovation. Innovation, of course, takes many forms. The term is applied to basic scientific breakthroughs, important commercial inventions, product modifications and new production techniques. All are important to society. Innovation, whether in the form of improved product quality and variety or production efficiency that allows lower prices, is a powerful engine for enhanced consumer welfare. By prohibiting private restraints that impede entry or mute rivalry, antitrust seeks to create an economic environment in which the entrepreneurial initiative that is the hallmark of the U.S. economy can flourish; it creates and maintains opportunities for bringing innovations to market.

Moreover, this nation's experience teaches that innovation comes from unpredictable sources -- from individuals and small firms as well as giant conglomerates. And this diversity in the sources of innovation is not limited to the 19th and early 20th centuries, when change arguably occurred less rapidly. If you compare the major firms in the computer and telecommunications industries in the 1950s, '60s, and '70s with the major firms today, you will see that rapid technological change can create opportunities for new entrants and individual achievement.

It wasn't IBM that launched the personal computer revolution, but rather a then-tiny upstart named Apple Computer. The PC revolution, in turn, has dramatically reduced the cost of compiling, processing and transmitting

information, taking away a significant cost advantage once held by larger companies and thus making it possible for tens of thousands of other companies outside the computer business to flourish.

The task of antitrust is not to prejudge winners but to make sure that private restraints do not narrow the potential sources of innovation or bar entry to markets by innovators. By preserving an economic climate that allows efficient sources of innovation to prosper, be they small or large, antitrust promotes the economic and socio-political values that have been the backbone of the success of the American economy.

An effective antitrust enforcement program promotes innovation by, among other things, reducing barriers to entry. When antitrust enforcement is a reality, potential entrants have less reason to fear market exclusion by existing firms. Antitrust enforcement can also act to prevent horizontal or vertical mergers that create non-efficiency based advantages for incumbent market leaders. For these and other reasons, potential entrants are more likely to invest the capital and effort needed for innovation when they have a chance to compete on the economic merits of their products or services.

We need not look solely to theory for evidence that antitrust enforcement promotes innovation. One need look no further than the government's landmark monopolization case against AT&T to see the critical role that antitrust enforcement plays in spurring innovation and investment. Prior to the lawsuit, most of the nation was served by an integrated monopolist that faced little or no rivalry in the various telecommunications markets in which it operated. Consumer choice was hardly the hallmark of the AT&T system -- improvements appeared at a pace dictated by AT&T and its

lengthy depreciation schedule, as opposed to the needs of business or residential customers.

The divestiture required by Judge Greene in 1984 separated the local telephone companies from AT&T's long-distance service and equipment manufacturing firms. Other equipment manufacturers now had an opportunity to sell their wares on the basis of quality, cost and efficiency to the divested local operating companies, AT&T's emerging long distance rivals, and users of telecommunications services. In terms of innovation, the results have been spectacular.

For example, in the early 1970's, Corning invented the fiber-optic cable and tried to sell this wonderful new product to AT&T. But AT&T was not interested. It was left to a consortium of small independent telephone companies, followed by MCI and Sprint, to lay down the fiber-optic cable -- which, of course, forms the existing backbone of the coming Information Superhighway.

Our enforcement activities in the merger area also demonstrate that antitrust enforcement has an important role in spurring innovation. In the last year, we challenged two mergers that we believed would have caused a decrease in innovation by reducing incentives to expend R&D dollars.

The Division filed suit against the proposed acquisition of General Motors' Allison Division by ZF Friedrichshafen, which would have combined their bus and truck automatic transmission businesses. Our concern over the transaction was not limited to those narrow product markets in which the two firms were competing at the time. Rather, one of our principal concerns was that the combined firm would have controlled most of the assets, world-wide, necessary for innovation in heavy duty truck and bus automatic transmissions. Because innovation was tightly linked to

possession of the productive capacity necessary to carry out R&D activities, and only these two firms possessed the necessary productive capacity, innovation would have been stifled by the merger. Our complaint therefore alleged an anticompetitive effect, not just in the specific goods markets that had been the subject of direct sales competition in the past, but in a market for innovation.

A similar concern influenced the filing of the Division's recent suit against Flow International's attempt to acquire Ingersoll-Rand's Waterjet Cutting Systems Division. Flow and Ingersoll-Rand are the two major U.S. producers of ultra-high pressure waterjet pumps, key components of waterjet systems used in industrial cutting applications. They compete head-to-head in innovation that leads to new and improved waterjet pumps, nozzles, cutting heads, abrasive delivery systems, and other components. The proposed acquisition would have created a combined company with a market share of 90 percent -- a virtual monopoly. We alleged that the acquisition would only have deprived customers of lower prices, but that it also would have substantially lessened technological innovation for waterjet pumps. The Division filed suit on April 4, and the parties abandoned the transaction less than a month later.

Our focus on innovation in the GM and Waterjet cases is an example of how we will continue to strive to protect competition in technology. We are concerned not only about monopoly effects or pricing, but also with the impact on innovation. We focus on technology because we view innovation as crucial to consumer welfare and believe that consumer welfare is enhanced when innovative diversity and competition are preserved. It also has international implications because technological innovation is the key to long-term success in international trade. The United States leads the world in R&D investment, and spends more in R&D than Japan, Germany, the

United Kingdom and France. It would be a great mistake, in my view, to promote antitrust policies and private arrangements that adversely affect America's leadership in R&D.

I don't want to leave the impression, by talking about instances in which the Division has blocked a transaction in order to protect innovation, that we are oblivious to the fact that many transactions promote innovation. Mergers may produce significant economies of scale or scope without harming competition. Mergers are frequently ways of bringing together complementary inputs. For example, one company may have great basic research capabilities and discoveries but little ability to develop them into commercial products, manufacture them efficiently, or market them effectively. Where that is the case, a merger with a firm that has strengths in development, manufacturing, or distribution may facilitate innovation. Antitrust analysis takes these complementarities into account.

I have argued so far that both our antitrust and intellectual property laws share a common objective: promoting innovation. But intellectual property, as the Federal Circuit has recognized in a number of decisions, can also be improperly invoked to the detriment of competition and the goal of technological progress. For example, holders of intellectual property rights may improperly use them to coordinate a cartel and suppress competition in alternative technologies or associated markets, to raise barriers to entry in other markets, or to extend the period of exclusion beyond the statutory term. If any of these events transpire, the result may be reduced output (including reduced U.S. exports), unsanctioned monopoly profits, and stifled innovation.

These consequences are significant, especially in the international context. They have a direct impact on U.S. exports, as well as on the U.S. domestic economy. A good

example of how our enforcement activities in intellectual property can have a beneficial impact is our recent consent degree with Pilkington Glass, which we filed three weeks ago -- the first non-merger intellectual property case brought by the Antitrust Division in fifteen years.

Pilkington, a British company, years ago licensed the major world float glass manufacturers to use its technology only in specified territories. These original licenses contained stringent territorial, use and sublicensing restrictions, together with grant-backs of improvements developed by the licensees, which substantially limited competition among the licenses and Pilkington.

Pilkington's licenses were hybrid patent/know-how licenses which did not terminate upon the expiration of the patents, but continued indefinitely until the licensee could prove that all of the licensed technology was publicly known. Pilkington then overclaimed what was "secret" as a way of deterring or inhibiting the ability of licensees and other rivals from inventing around whatever legitimate intellectual property rights it possessed. Pilkington also entered into other agreements, including export limitations, with its licensees outside of and apart from the licenses as a way of limiting and controlling competition in glass markets.

As a result of the licensing agreements, United States companies were prohibited from exporting their own glass manufacturing technology, and that kept American companies from building glass-making plants overseas. This hurt United States output, innovation, and jobs.

In sum, the Pilkington case is a prime example of a licensing arrangement that imposed restraints on competition long after such restraints could be reasonably necessary to the advancement of the technology.

The proposed settlement, if adopted by the District Court, would prohibit Pilkington from improper use of intellectual property rights and would allow U.S. firms to compete for over 50 float glass plants that are expected to be built around the world. We estimate that this could result in an increase in U.S. export revenues of anywhere between \$150 million and \$1.25 billion over the next six years.

The Pilkington case is also significant because it is the first case under a 1992 policy change that permits the Justice Department to challenge foreign business conduct that harms U.S. export trade. In 1982, Congress clearly defined the jurisdictional scope of the Sherman Act to include enforcement against foreign companies whose conduct adversely affected U.S. domestic commerce and export trade. However, in 1988, "footnote 159" of the 1988 International Guidelines unilaterally renounced that Congressional directive by stating that anticompetitive conduct would be challenged only if there was direct harm to U.S. consumers, and that harm to U.S. exports would not, by itself, be a sufficient basis for filing a lawsuit. To his immense credit, my predecessor Jim Rill withdrew footnote 159 in 1992, and stated that the Department will use its enforcement powers in appropriate circumstances to preserve the ability of American enterprises to compete in international markets for U.S. export business. The proposed settlement in the Pilkington case is an example of how antitrust enforcement can open new markets for American businesses exporting high-tech services.

Sound antitrust enforcement can serve as a catalyst to technological innovation and promote U.S. competition here and

abroad. To have that result, however, our policy must be clear and coherent. To that end, six months ago we formed a Division task force, chaired by Deputy Assistant Attorney General Richard Gilbert, to formulate our policy and to draft new intellectual property Guidelines. These Guidelines, as I mentioned, will be published in the Federal Register shortly for public comment. I will now outline three major principles that will be reflected in the new Guidelines.

The bedrock principle of our enforcement policy is that intellectual property is treated the same under the antitrust laws as is any other property. That is not to say that intellectual property is in all respects the same as any other form of property. Intellectual property has important characteristics that distinguish it from many other forms of property. In addition, we recognize that there are clear and important differences in the purpose, extent, and duration of protection provided under the intellectual property regimes of patent, copyright, and trade secret. However, these characteristics and differences can be taken into account by standard antitrust analysis, and do not require the use of fundamentally different principles.

The intellectual property laws create property rights that permit the owners of intellectual property to profit from the use of their property by excluding others. These rights are similar to the rights enjoyed by owners of other forms of private property. As with other forms of private property, certain acquisitions or uses of intellectual property may have anticompetitive effects against which the antitrust laws can and do protect. Intellectual property is thus neither particularly free from scrutiny under the antitrust laws, nor particularly suspect under them.

A second major principle underlying our intellectual property policy is that we will not presume market power in

the antitrust context solely from the existence of an intellectual property right. Whether such market power in fact exists depends on what substitutes are available. If a specific form of intellectual property does confer a significant competitive advantage on its owner, that advantage is no more in conflict with the antitrust laws than one created by any other asset that enables its owner to earn supracompetitive profits. Judge Learned Hand's statement in the *Aloca* case in 1945 that the Sherman Act is not violated by the attainment of power solely through "superior skill, foresight and industry" remains apt today with respect to the types of innovation protected by intellectual property rights.

A third guiding principle is that licensing is very important to the economy and that the antitrust laws should encourage procompetitive licensing. We recognize that licensing, cross-licensing or otherwise transferring intellectual property facilitates its integration with complementary factors of production and encourages the sharing of technology. This can lead to a more efficient exploitation of intellectual property, which benefits consumers by accelerating the reduction of costs and the introduction of new products resulting from the intellectual property. Licensing arrangements can promote economic welfare by integrating complementary intellectual property and avoiding costly infringement litigation. By potentially increasing its expected returns, licensing also can increase the incentive to invest in creating intellectual property. In addition, we also recognize that field-of-use, territorial and other limitations on intellectual property licenses may serve procompetitive ends in allowing the licensor to exploit its property as efficiently and effectively as possible.

Outside of a few narrow per se rules -- like blatant price fixing and certain tying arrangements -- most transactions in the intellectual property area will be

evaluated under the Rule of Reason, which weighs the likely procompetitive benefits against potential anticompetitive effects. We believe that our policy is designed to encourage the development of innovation and complementary inputs.

While we recognize that intellectual property licensing arrangements are generally welfare enhancing and procompetitive, I would be remiss if I did not say we also know that licensing arrangements may sometimes adversely affect competition. A good example would be the Pilkington case, where territorial restraints were imposed that had no significant relation to protection of the intellectual property and that impeded the ability of firms -- including U.S. firms -- to compete using their own technology. Other examples may include licensing restrictions with respect to one market that may reduce competition in an adjacent market by foreclosing access to or raising the price of an important input.

I hope this summary of our current thinking on the basic tenets of our enforcement policy has been helpful. We will remain engaged in our enforcement activities in this area. Together we can ensure that America will make the fullest use of her intellectual capital and will continue to have the greatest incentives to invest in additional technological progress. Thank you.