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2 and
3 UNITED STATES DEPARTMENT OF JUSTICE
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7 SHERMAN ACT SECTION 2 JOINT HEARING
8 UNDERSTANDING SINGLE-FIRM BEHAVIOR:
9 MISLEADING AND DECEPTIVE CONDUCT SESSION
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15 HELD AT:
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16 Gil Ohana

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1 P R O C E E D I N G S

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3 MR. DAGEN: Okay, good morning, everybody. I am
4 Richard Dagen, Special Counsel to the Director of the
5 Bureau of Competition and one of the moderators for this
6 session. My co-moderator is Hill Wellford, Counsel to
7 the Assistant Attorney General for Antitrust at the
8 Department of Justice. Before we start, I need to cover
9 a few housekeeping matters.
10 First, please turn off your cell phones,
11 BlackBerries and any other devices. Second, the
12 restrooms are outside the double doors and across the
13 lobby. There are signs to guide you. Third, one safety
14 tip, particularly for visitors, in the unlikely event
15 the building alarms go off, please proceed calmly and
16 quickly as instructed. If we must leave the building,
17 exit the New Jersey Avenue exit by the guard's desk, and
18 please follow the stream of FTC people to a gathering
19 point and await further instruction. Finally, we
20 request that you not make comments or ask questions
21 during the session. Thank you.
22 Now, today we are honored to have assembled a
23 distinguished panel of practitioners, consultants and
24 professors who are well versed in the issues we will
25 tackle today involving misleading and deceptive conduct.

1 The hearing will be organized as follows: First, we
2 will hear an approximately 15-minute presentation from
3 each panelist. We will likely break after the fourth
4 panelist speaks, and after the break, hear from our
5 final two speakers. After the presentations, we will
6 have a round table discussion moderated by Hill Wellford
7 and me.
8 Our panelists today are Susan Creighton, who is
9 a partner at Wilson Sonsini Goodrich & Rosati and a
10 former director of the FTC's Bureau of Competition;
11 Preston McAfee, who is the J. Stanley Johnson Professor
12 of Business Economics and Management at the California
13 Institute of Technology; Gil Ohana, who is the Director,
14 Antitrust and Competition, Cisco Systems; Richard Rozek,
15 who is a senior vice president, NERA Economic
16 Consulting; Michael Brockmeyer, who is a partner at
17 Frommer Lawrence & Haug and an Adjunct Professor of Law
18 at the University of Maryland School of Law; and George
19 Cary, who is a partner at Cleary Gottlieb Steen &
20 Hamilton and a former Deputy Bureau Director of the
21 FTC's Bureau of Competition.
22 I want to thank the FTC and DOJ Section 2 staff
23 for organizing this session. This is the last Section 2
24 hearing for 2006, but the hearings will continue during
25 the first few months of 2007, so be sure to check the

1 agencies' web sites for updates.
2 Second, I want to explain why a session entitled
3 Misleading and Deceptive Conduct is, in fact, a session
4 about Section 2 of the Sherman Act and not a hearing
5 being held by the FTC's Bureau of Consumer Protection.
6 Deceptive conduct is a type of exclusionary conduct that
7 has been the basis for antitrust liability under Section
8 2. The Federal Trade Commission defined deception in
9 1983, noting that the FTC "will find deception if there
10 is a representation, omission or practice that is likely
11 to mislead the consumer acting reasonably in the
12 circumstances to the consumer's detriment."
13 In In re Rambus, a matter involving conduct
14 before a standard-setting organization, the Commission
15 explained that the policy statement could be applied to
16 a Section 2 analysis, although it did not directly
17 equate the policy statement's definition of deception
18 with exclusionary conduct under Section 2. Consistent
19 with our general policy to avoid discussing cases during
20 the hearings that are currently in litigation, and
21 because the Rambus matter is still in administrative
22 litigation and there has not been a final appealable
23 judgment, we will not be discussing this case today.
24 There are a variety of scenarios under which
25 deceptive and misleading conduct may form the basis of a

1 Section 2 antitrust violation, and this hearing is
2 designed to address many of them. Deception also may
3 encompass fraud, bad faith, falsehoods,
4 misrepresentations and misleading conduct. These terms
5 are related and sometimes used interchangeably. Such
6 conduct can occur in both the private and public sector.
7 Certain business torts and standard-setting activity may
8 provide the basis of Section 2 liability.
9 In one recent case, Conwood versus United States
10 Tobacco, the Sixth Circuit upheld a $1 billion treble
11 damages award. The allegations of exclusionary conduct
12 in Conwood included misrepresentations of sales data to
13 retailers as well as the destruction of competitors'
14 products and displays.
15 In United States versus Microsoft, the D.C.
16 Court of Appeals found that Microsoft engaged in
17 exclusionary conduct in violation of Section 2 when it
18 deceived Sun Microsystems and independent software
19 developers by offering them a set of Java implementation
20 tools that ostensibly would enable them to develop
21 cross-platform applications but could be executed only
22 by Microsoft's version of the Java runtime environment
23 for Windows.
24 Misleading and deceptive conduct in the context
25 of abuse of governmental processes can also be the basis

1 for Section 2 liability. Such cases have included FDA
2 Orange Book listings and fraud on the Patent Office.
3 Now I would like to turn it over to Hill for a
4 few remarks.
5 MR. WELLFORD: Good morning. My name is Hill
6 Wellford. I am counsel to AAG Tom Barnett. The FTC and
7 DOJ are jointly sponsoring these hearings today to help
8 advance development of the law concerning the treatment
9 of unilateral conduct under the antitrust laws. This is
10 one of the most controversial areas even within Section
11 2, which is controversial enough on its own, and I think
12 we should have a very good panel today. I have seen
13 some of these presentations that have come in, and I am
14 very much looking forward to the remarks that will be
15 presented by the panel. Thanks to my colleagues at the
16 FTC and the Division for organizing this. I will hand
17 it back over to Rich.
18 MR. DAGEN: So, I would like to introduce your
19 first speaker. Susan Creighton, as I mentioned before,
20 is a partner at Wilson Sonsini. Between 2001 and 2006,
21 she served at the Federal Trade Commission first as
22 Deputy Director and then as Director of the Bureau of
23 Competition. While at the FTC, she played a key role in
24 developing antitrust policy and made important
25 contributions about, among other things, the

1 intersection of antitrust and intellectual property.
2 She is a frequent author of antitrust articles,
3 including a 2005 Antitrust Law Journal article entitled
4 "Cheap Exclusion" dealing with many of the issues we
5 will be discussing today.
6 Susan?
7 MS. CREIGHTON: Good morning. Let's see if I
8 can figure out how to make this thing move. That
9 worked, okay.
10 So, courts and enforcers long have recognized
11 that deception can constitute unlawful exclusionary
12 conduct under Section 2 of the Sherman Act. With
13 respect to deception in the context of private business
14 arrangements, probably the two most recent prominent
15 decisions are the D.C. Circuit decision in Microsoft and
16 the FTC's decision in Rambus. The potential for
17 deception in government proceedings to serve as the
18 basis for Section 2 liability is reflected in cases
19 stretching as far back as the Supreme Court's decision
20 in Walker Process and more recently has been a major
21 part of the FTC's enforcement agenda, as Rick mentioned,
22 in cases such as UNOCAL and the Orange Book listing
23 cases.
24 In my view, these cases are correct in holding
25 that deception can constitute a basis for finding

1 exclusionary conduct under Section 2. Indeed, as my
2 co-authors and I argued in the article that Rick
3 referred to in the Antitrust Law Journal entitled "Cheap
4 Exclusion," deception and other forms of cheap exclusion
5 are potentially a very effective form of anticompetitive
6 conduct and properly should be a core focus of
7 enforcement efforts by the FTC, the Antitrust Division
8 and the state enforcement agencies.
9 In particular, in our article, we highlighted
10 three characteristics of such cheap exclusion, including
11 deception. First, it is cheap in the sense that it
12 costs little to the firm engaging in it. False
13 statements made during a governmental standard-setting
14 proceeding may be virtually costless, for example,
15 particularly for a firm that would have participated in
16 the regulatory proceeding in any event. These de
17 minimus costs compare favorably to the high costs that a
18 firm might incur, for example, through the low-cost
19 pricing or potentially strategies such as exclusive
20 dealing.
21 Second, the conduct also is cheap in the sense
22 of lacking any redeeming virtue. Deceptive conduct
23 unambiguously fails to enhance any party's efficiency,
24 provides no benefits short or long term to consumers,
25 and its economic effect produces only costs for the

1 victims and wealth transfers to the firms engaging in
2 the conduct fully apart from its potential contribution
3 to market power.
4 Finally, it is also cheap in the relative sense
5 that it is a strategy where the costs are often likely
6 to be far outstripped by the anticompetitive benefits.
7 As the Antitrust Division explained in its business
8 review letter, for example, "Early in the
9 standard-setting process, standard-setting members often
10 can choose among multiple substitute technological
11 solutions, some of which may be patented. Once a
12 particular technology is chosen and the standard is
13 developed, however, it can be extremely expensive or
14 even impossible to substitute one technology for
15 another." Misrepresentations that enable a firm to
16 charge higher discriminatory royalty rates after lock-in
17 therefore may enable the firm to enjoy substantial and
18 durable market power.
19 Because deceptive conduct ordinarily has no
20 efficiency or other procompetitive benefits, other forms
21 of cheap exclusion do not provide the same type of
22 trade-off that we see with respect to most other forms
23 of exclusionary conduct that have been the subject of
24 the previous hearings, predatory pricing, bundling,
25 exclusive dealing and the like. With respect to these

1 forms of conduct, it is generally recognized that they
2 will often, maybe even overwhelmingly often, be
3 procompetitive rather than anticompetitive. The
4 challenge, therefore, is to distinguish the times when
5 the conduct might be anticompetitive without unduly
6 chilling the procompetitive conduct.
7 With respect to deceptive or other opportunistic
8 conduct, however, there is no similar concern that we
9 will be unduly chilling deception or opportunism. In
10 fact, sort of phrased that way, I do not think we
11 generally sort of think of being concerned about
12 chilling deception. In this context, cheap exclusion
13 may be viewed as something like the Section 2 analog to
14 Section 1 price fixing; that is, we are not unduly
15 concerned with overdeterrence of this behavior, and it
16 is at the same time at the far end of the spectrum for
17 Section 2 purposes from predatory pricing.
18 If there is a category of conduct that we are
19 particularly concerned not to chill under Section 2, it
20 is price cutting. With respect to misrepresentations
21 and deception, by contrast, we have and should have no
22 such scruples.
23 Screening tests designed to find the single
24 exclusionary goat in the vast herd of procompetitive
25 sheep, therefore, are not well suited and should not be

1 applied to exclusionary fraud or deception. The profit
2 sacrifice test, for example, originally conceived as a
3 means to screen out legitimate pricing behavior, does
4 not work well when applied to conduct that is not
5 legitimate, whether or not it is exclusionary.
6 For example, fraudulent regulatory filings that
7 can be made at de minimus costs may have powerful
8 exclusionary effects due to the operation of extrinsic
9 legal schemes. At the same time, such conduct also may
10 be profitable even if it does not result in the creation
11 of durable market power by harming competitors and
12 generating profits for the filing firms, yet the mere
13 fact of the profitability of this illegitimate behavior
14 tells us nothing about whether the behavior or the
15 fraudulent filing is legitimate efficiency-enhancing
16 behavior.
17 Now, if the balancing question typically raised
18 regarding Section 2 conduct is not present here, what
19 other concerns are raised regarding exclusionary fraud
20 or deception? It seems to me that there are three
21 concerns that are raised most frequently. The first is
22 causation. This issue underlies a considerable portion
23 of the Commission's legal analysis in Rambus, for
24 example, and I'll return to that. The second is that
25 antitrust should not be used as a kind of ex post

1 gap-filler for poorly written standard-setting rules or
2 legal regulations. And the third is that we should not
3 use antitrust where other laws, such as business torts
4 and contract law, already can be used to reach and
5 prohibit the conduct.
6 Let me address each of these three objections
7 briefly in turn. First, with respect to causation, it
8 seems to me that contrary to the concern about causation
9 often expressed in this area, exclusionary deception, in
10 fact, often occurs in circumstances where the
11 environment is, in fact, conducive to the acquisition or
12 maintenance of durable market power. Indeed, for
13 deceptive conduct in the government context, it seems to
14 me that this is often likely to be the rule rather than
15 the exception.
16 The reason is simple. If the exclusion operates
17 by force of law, the exercise of market power will not
18 induce new entry, and the entry barriers created by the
19 need to change laws or regulations may be formidable
20 indeed. The UNOCAL case, for example, highlights these
21 effects. Now, that's in the government context.
22 In the private context, as the Commission
23 discussed in Rambus, profitable private ventures may
24 also often be conducive to the use of deception to
25 acquire or maintain durable market power. In instances

1 where business relations are characterized by
2 cooperation rather than competition, for instance, the
3 Java development program in Microsoft or in instances of
4 private standard-setting activity, deception may be
5 difficult to deter or counter, and the resulting
6 lock-in, especially in network industries, may be
7 difficult or impossible to overcome once the deception
8 has been detected.
9 Now, in this regard, deceptive advertising,
10 where the statements are both ascertainable and
11 falsifiable, may actually be the exception rather than
12 the rule. In Caribbean Broadcasting, for example, the
13 alleged deceptive statement was one that was made
14 publicly, and it would appear to be one that would be
15 readily falsifiable. Did the company's broadcast, in
16 fact, reach the entire Caribbean region or not? That
17 seemed to be an answer that you probably could pretty
18 much figure out with a couple of guys and radios.
19 Now, by comparison, in Conwood, if I understand
20 the allegations correctly, the alleged deceptive
21 statements were made in private communications to
22 retailers. It is unclear how or when the plaintiff
23 would have been able to learn of them, and hence, to
24 counteract them.
25 One might also consider a statement that is less

1 readily falsifiable. For example, statements claiming
2 patent infringement by a competitor's product without
3 any identification of the particular patents in issue or
4 anything sort of as formal as some kind of warning
5 letter that would make it possible to respond to the
6 allegation might be the kind of tipping event you could
7 expect potentially to have a forceful impact in network
8 industries.
9 Now, the second concern raised regarding
10 exclusionary deception is what I have called the
11 gap-filling problem. The concern here, as I understand
12 it, is that antitrust is effectively being used in these
13 circumstances to take care of problems that could have
14 been solved ex ante through more careful drafting,
15 either the Orange Book regulations or the
16 standard-setting rules.
17 Now, here I raise with some trepidation as a
18 lawyer on a panel with economists who may, in fact,
19 provide a more subtle understanding of this point, it
20 seems to me that the insight of transaction cost
21 economics is applicable here, and I have up here a quote
22 from Oliver Williamson. "The general rubric out of
23 which transaction cost economics works is that of hazard
24 mitigation through ex post governance. It being the
25 case that all complex contracts are unavoidably

1 incomplete, the fiction of comprehensive contracting,
2 which concentrates all of the contracting action on ex
3 ante incentive alignment, is untenable."
4 Now, I have also referred in my slides here and
5 also in the "Cheap Exclusion" article by analogy to an
6 article written some time ago by former FTC chairman Tim
7 Muris regarding the judicial doctrine of the duty of
8 good faith and fair dealing. His point, as I understand
9 it, in the article was that parties to a contract cannot
10 adequately defend themselves ex ante against
11 opportunistic conduct that undermines the parties'
12 legitimate expectations, perhaps even the purpose of the
13 contract, at least not without incurring wasteful and
14 inefficient transaction costs of the type that
15 Williamson was describing.
16 So, the judicial imposition of good faith and
17 fair dealing is an efficient means of protecting parties
18 against conduct that is contrary to their legitimate
19 expectations but not necessarily contrary to the precise
20 language of the contract.
21 By analogy, the antitrust laws can and should
22 serve to protect against deceptive or opportunistic
23 misuse, for example, of collaborative ventures such as
24 standard-setting organizations where such conduct
25 defeats the very purpose of such arrangements and that

1 which makes them acceptable under the antitrust laws.
2 That intuition, I think, for example, is what the
3 Supreme Court was driving at when it said in Allied Tube
4 that, "Private standard-setting by associations is
5 permitted under the antitrust laws only on the
6 understanding that it will be conducted in a nonpartisan
7 manner offering procompetitive benefits."
8 Now, although standard-setting organizations can
9 and should exercise self-help to the extent possible,
10 the insight of transaction cost economics is that no
11 amount of ex ante bargaining can ever perfectly secure
12 collaborative ventures or other government regulations,
13 such as the Orange Book, against opportunism in
14 circumstances where it turns the purpose of the
15 collaboration or the regulation on its head and in a way
16 that it threatens the creation of durable market power.
17 Moreover, in other contexts, such as the Java
18 development in Microsoft, the collaboration will not
19 even be pursuant to elaborate written contracts. In
20 such circumstances, antitrust law in my view properly
21 provides part of the ex post governance structure that
22 helps ensure ex ante that such collaborations and
23 regulations achieve their intended procompetitive
24 purposes.
25 Now, finally, sometimes the question whether

1 deceptive exclusion should be subject to Section 2 gets
2 posed wrongly in my view as whether the conduct at issue
3 is a business tort, and if it is, why then do we need to
4 subject it to the antitrust laws? I think that this
5 asks the question through the wrong end of the
6 telescope. The right question to ask is, is an
7 inefficient exclusionary act that is likely to have
8 caused market power nonetheless excused under Section 2
9 because it also violates another law or statute?
10 Now, the reason it is important to ask the right
11 question is the old true saying, the wrong answer is
12 what the wrong question begets. Here, asking first
13 whether the conduct is tortious and then why do we need
14 antitrust is likely to be misleading in at least three
15 ways.
16 First, these business torts and contract rights
17 vindicate the rights of the wrong people. In a
18 standard-setting organization, for example, we are not
19 concerned ultimately with the rights of the
20 standard-setting organization or its participants, but
21 consumers. As Ted Gephart has written about,
22 standard-setting organizations and their participants
23 may or may not have interests that coincide with those
24 of consumers, but simply because they might be
25 indifferent to the anticompetitive consequences of the

1 deceptive conduct, for example, because they will be
2 able to pass through price rises to consumers, does not
3 address what antitrust is concerned with, namely,
4 whether the conduct harms consumers.
5 Now, similarly, business torts and contract law
6 provide the wrong measures of causation and harm. A
7 standard-setting participant who is able to pass along
8 price increases may not have been harmed and should not
9 be able to recover for the nonetheless real harm that
10 consumers will have suffered.
11 Finally, business torts may have elements that
12 do not fit well with the proper issue from an antitrust
13 perspective, or conversely, may be missing elements
14 necessary to answer the antitrust claim. The intent
15 element in fraud, for example, may or may not be apt to
16 the proper antitrust question in a particular factual
17 setting.
18 Now, underlying this question, I think,
19 ultimately really is a different issue, which is the
20 hostility to private rights of action under Section 2,
21 particularly their treble damage provisions, and a
22 concern regarding unjustified suits. That issue,
23 however, in my view properly should be dealt with
24 directly and not by wrongly manipulating substantive
25 standards under Section 2.

1 For the reasons that I have explained, I think
2 that, in fact, this is an area that should be a
3 priority, not a backwater for federal and state
4 antitrust agencies. The importance of the substantive
5 area should not be obscured or the barriers to effective
6 enforcement heightened by an effort to cut off private
7 litigation whose flaws lie elsewhere, not in their
8 substantive antitrust claims, but rather, in procedural
9 rules that govern private Section 2 actions.
10 Thank you very much.
11 (Applause.)
12 MR. DAGEN: Thank you, Susan.
13 Our next speaker is Preston McAfee. He's the
14 J. Stanley Johnson Professor of Business Economics and
15 Management at the California Institute of Technology
16 where he teaches business strategy, managerial
17 economics, and principles of economics. Preston is the
18 author of over 70 articles published in scholarly
19 economics journals and co-author of the book Incentives
20 in Government Procurement. He served as one of four
21 economists who edit the American Economic Review for
22 over nine years.
23 Preston?
24 DR. McAFEE: Thank you. Thank you, Susan, for
25 actually providing the lead-in for what I would like to

1 talk about today, and let me also apologize for being
2 still on California time and so only about 60 percent
3 awake.
4 So, I would like to talk about the right of
5 private action under the antitrust laws and connect that
6 to deception and fraud as follows. Whatever is decided
7 about deceptive practices and the right to sue under the
8 antitrust laws will be abused in private suits if those
9 are permitted, and let me warm up with VeriSign. So,
10 VeriSign is the registrar of .com and .net, and in 2003,
11 they began redirecting mistyped addresses to their own
12 advertising site. The ISPs objected and asked the ruler
13 of the internet to stop the practice, and VeriSign
14 contended that that was an illegal conspiracy. The
15 judge threw this out, which I think was the right
16 answer.
17 One thing that is a really interesting question
18 about this particular antitrust suit is actually, what
19 is somewhat of a principle, I guess, is it is often hard
20 to fit modern industries into traditional economic
21 analysis of antitrust, and this is a really nice poster
22 child for that, because what is the quantity here? Is
23 it the number of mistyped addresses? Well, that is
24 something that is not affected by anyone's behavior,
25 because that is just purely, you know, when consumers

1 make a mistake will determine that.
2 On the other hand, you might think it is the
3 number of advertisements, or in this case, is it the
4 number of Viagra ads that are produced? Well, here is a
5 situation where, in fact, we would like to reduce the
6 quantity. That is, it would be welfare-enhancing to
7 actually reduce the quantity that is produced by the
8 industry. It does not quite stop there.
9 So, another company that buys expired domains
10 and then redirects them to its own advertising site sued
11 VeriSign, that is, the plaintiff in the previous
12 antitrust suit, saying that the existence of VeriSign's
13 site finder itself violated the antitrust laws, and that
14 suit, last time I looked, which was a week ago, seems to
15 still be continuing. So, one thing is is that these
16 suits concern the same behavior, that is,
17 sitefinder.com, one saying that it was required and the
18 other saying that it is prohibited by the antitrust
19 laws, and so it makes for an interesting challenge.
20 So, here are the things I would like to talk
21 about. I have already talked about one example, and I
22 am going to mention a couple more. I want to then talk
23 about some research on for what purposes are private
24 antitrust claims brought, who has an incentive to sue,
25 and report on some research on that, and then conclude.

1 The Colorado Chiropractic Council sent hospitals
2 requests for privileges and included in their request
3 the threat of a lawsuit if denied. Nine of the
4 hospitals did not admit the Colorado Chiropractic
5 Council, and these hospitals were all, in fact, sued for
6 restraint of trade. The suit was thrown out, but the
7 message I want to bring to this is 21 hospitals admitted
8 them, and while it is not demonstrated, it appears that
9 the threat of an antitrust suit was, in fact, an
10 effective threat.
11 Antitrust actions outnumber or private suits
12 outnumber government suits nine to one. Some of the
13 reasons that they are given, I spoke with an attorney
14 who says he tried to convert every contract suit into an
15 antitrust suit as his first action, because it gives him
16 access to treble damages, recovery of legal fees, and it
17 is easier to survive summary judgment. So, private
18 actions have grown. Canada, actually, did not permit
19 private litigation until 1976, and they are still rare,
20 probably because they do not have treble damages.
21 So, the general idea which I think Susan
22 reflected for me is that the incentives for private
23 antitrust litigation are not guided by consumer welfare.
24 The firms bringing the suit, consumer welfare generally
25 is not their goal or motivation. So, what I want to

1 look at is, what are the actual motives of firms engaged
2 in private antitrust action and assess to what extent
3 the law can be used strategically, and then hopefully
4 that will give us some insight into crafting the laws to
5 minimizing the damage that is actually brought.
6 Some of the uses to which the antitrust laws are
7 brought -- private suits are put are harassment, harm
8 and extortion, and harassment and harm can actually be
9 used to induce cooperation, and this is especially
10 effective because it is often cheaper to sue than it is
11 to defend, and if you want to ensure cooperation, what
12 you want is a punishment that is easy to mete out but
13 expensive for the punished, and if it is symmetric, this
14 is actually the economic theory of cooperation or
15 collusion, actually, the same theory, suggests that that
16 is the kind of punishment you would like to use. In
17 addition, extortion reduces the returns to investment.
18 That is clearly chilling -- chilling effect on
19 investment.
20 Surveying a large number of private antitrust
21 suits, we have come up with seven different reasons for
22 private litigation, and I have color-coded them to what
23 extent they are opposed to the interests of consumers.
24 So, two quite common reasons are extorting funds from a
25 successful rival, and I want to especially point to

1 follow-on suits. So, when the Government brings a suit,
2 generally there is an entire group of people who follow
3 on. Microsoft, of course, has been subject to many of
4 those follow-on suits.
5 In addition, changing the terms of a contract,
6 antitrust suits can be effective means of doing that on
7 occasion, and as I said, some contract attorneys prefer
8 antitrust suits because they think that it makes the
9 defendant more likely to settle. Something that is
10 speculative on our part is that it can be used to punish
11 noncooperative behavior. Of course, no one is going to
12 admit to this, because by and large you have then
13 admitted to violating the antitrust laws directly, but
14 from a theoretical perspective, that would be a reason
15 for private antitrust litigation.
16 Responding to an existing lawsuit and preventing
17 a hostile takeover are common reasons. These do not
18 actually have any direct negative effect on competition.
19 They depend on whether the existing lawsuit was itself
20 pro or -- procompetitive or not or the existing hostile
21 takeover, and I would point to those as being in some
22 sense neutral. Where the antitrust -- where private
23 suits turn the antitrust laws on their head is when they
24 discourage the entry of a rival, such as in the Utah Pie
25 case, or that they prevent a successful firm from

1 competing vigorously.

2 Now, this, of course, is one of Microsoft's

3 defenses. I am not going to comment on that directly,

4 but independent service organizations often bring these

5 suits to prevent manufacturers from offering service and

6 competing successfully. So, in that sense, they can

7 quite turn the antitrust laws on their head.

8 Now, let me turn to some theoretical research.

9 This is not based on the survey of antitrust suits. The

10 question is, who has the incentive to actually bring a

11 private antitrust suit that is, in fact,

12 anticompetitive? And to assess that, we look at a

13 procompetitive action. So, this is a cost-reducing

14 action that will give a firm an advantage in the

15 marketplace versus an anticompetitive action, so this is

16 raising your rivals' costs without lowering anyone's

17 costs, and ask, holding constant the likelihood of

18 prevailing, who would benefit more from bringing the

19 suits?

20 And we actually, in the context of the sort of

21 standard work horse model, the Cornell model, the

22 standard economic model that is used most frequently in

23 antitrust evaluation, we find something I think quite

24 surprising, which is that it is the small firm in a

25 dispersed market who actually relatively benefits from

1 bringing an antitrust suit that is anticompetitive
2 relative to a procompetitive suit, and the reason for
3 this is the loss from a procompetitive rival's action
4 actually gets larger as the number of firms grows,
5 whereas the loss from an anticompetitive action
6 decreases as the number of firms grows, so that in the
7 limit, it is the small firm and not the large firm who
8 tends to bring the action.
9 So, to conclude, antitrust laws are often used
10 not to encourage competition -- at least private
11 antitrust suits -- but to reduce the level of
12 competition. Clearly an outright ban on private
13 antitrust litigation would solve that problem, but it
14 may create other problems that are worse. Some
15 alternatives may actually improve the situation as it
16 stands today.
17 One would be a gate-keeper, using government
18 agencies as a gate-keeper for private litigation, but I
19 am actually leery of that as a solution mainly because I
20 judge the EEOC to be a failure as a gate-keeper in
21 employment, and the gate-keeper model has not worked
22 very well.
23 One could also ask the agencies to weigh in on
24 private litigation, and that may have more of an effect.
25 Another proposal is to allow for additional support

1 beyond what is already created, in particular financial
2 support for agency litigation. That, of course, risks
3 capture and so would be a risky strategy for different
4 reasons. Something that -- modeling in Canada, you have
5 a -- there is a -- is decoupling the damages from the
6 awards. It may be that you want to have high damages as
7 a way of deterring behavior but low awards to reduce the
8 number of lawsuits, and there are plenty of worthy
9 agencies who would love to have the difference between
10 the damages and awards.
11 And then finally, something that from my own
12 experience in litigation I would find useful is to
13 provide experts to the court to reduce the uncertainty
14 associated with antitrust suits.
15 Let me conclude with three remarks on deceptive
16 practices. One is is that not every misleading
17 statement is intentional. There are many
18 well-intentioned corporations that make mistakes, and
19 the law should not have zero tolerance. So, this is in
20 some sense a counter to remarks of Susan's, that there
21 is no downside. There are statements that are made.
22 Generally, if you run a corporation, it is hard to
23 ensure zero probability of a misleading statement ever
24 being made. People have -- make errors on occasion.
25 One of the things I would say about Oliver

1 Williamson is that reading Oliver Williamson is very
2 much like reading the Bible. When you read it
3 selectively, he provides support for every point of
4 view.
5 The second point that I would like to make is
6 that traditional economic analysis where a market -- and
7 by that I mean the analysis of antitrust -- where
8 markets are either monopolies or competitive, is the
9 sort of general situation, that kind of model is very
10 poorly suited to evaluating deceptive practices, and
11 there are lots of -- the problem is, often it is the
12 case that you can have a large effect on a small number
13 of people or a small effect on a large number of people,
14 and then what seems like an inconsequential difference,
15 so a small compatibility problem which is easily
16 remedied may still be fatal if it is something that
17 consumers will not remedy. These are situations where
18 it is not either a monopoly or a competitive
19 marketplace, and as a result, we in some sense need to
20 bring new economic models to the evaluation of deceptive
21 practices.
22 And then finally, I also want to say, in my
23 view, the patent system is broken. The system itself is
24 anticompetitive. It creates entry barriers. Many firms
25 cannot enter because -- so, firms with a good idea, who

1 have invented a new technology and go and get it
2 patented, find that because there are many patents that
3 have some similarities, they are blocked from entry by
4 existing patent pools. Patent pools, in addition, have
5 the effect of encouraging collusive conduct.
6 With a broken patent system -- and this, I
7 think, echos a point that Susan made -- I do not think
8 it is appropriate to try to fix the patent system using
9 the antitrust laws. Instead, it would be desirable to
10 fix the patent system directly. So, let's craft
11 antitrust laws that promote competition and a patent
12 policy that justly rewards the efforts to innovation.
13 Thank you.
14 (Applause.)
15 MR. DAGEN: Our next speaker is Michael
16 Brockmeyer. He's a partner at Frommer Lawrence & Haug,
17 where his practice concentrates on antitrust and
18 consumer protection law with particular emphasis on
19 intellectual property financing agreements and the
20 pharmaceutical industry. Before entering private
21 practice, Michael served as chair of the Multistate
22 Antitrust Task Force of the National Association of
23 Attorneys General and was a chief of Maryland's
24 Antitrust Division. He is a frequent author and
25 lecturer on antitrust matters, and he is also an Adjunct

1 Professor at the University of Maryland School of Law,
2 teaching antitrust law.
3 DR. BROCKMEYER: Thanks, Rick. Good morning,
4 everyone.
5 For my opening remarks this morning, I want to
6 focus on abusive governmental processes, in particular
7 with respect to deception in the intellectual property
8 setting, and then I am going to briefly touch on
9 tortious conduct.
10 I find it helpful, however, that before going
11 into those subjects, we should remind ourselves of
12 certain basic principles that should apply when we look
13 at any one of the subjects that we are talking about,
14 and so, for example, and what we take for granted today
15 I would assume, everyone, that aggressive competition on
16 the merits serves consumer welfare. Even if done by a
17 monopolist, competition on the merits is not
18 exclusionary. If we do not permit that, then we deprive
19 consumers the benefit of that competition.
20 Now, that is a principle that has become well
21 accepted in antitrust law, but we must remember that
22 that principle is not one that necessarily underlies
23 certain state laws that deal with deception or tortious
24 conduct.
25 The antitrust laws should not provide a remedy

1 for conduct that violates the common law or another
2 statutory scheme and injures individual competitors
3 unless the conduct substantially harms the competitive
4 process. In my view, such conduct that violates the
5 common law or another statutory scheme is not
6 competition on the merits, but the question is, is
7 whether often the conduct is sufficient enough to say
8 that it harms the competitive process.
9 In my view, the principle should be that that
10 conduct substantially harms the competitive process when
11 it allows, permits, durable pricing above competitive
12 levels or there exists a dangerous probability that such
13 supra-competitive pricing will occur. In my view, when
14 you have this sort of conduct, the competitors, the
15 injured competitor, cannot be passive. The competitor
16 must have attempted to counteract, must have done so in
17 a reasonable manner evaluated in the context of what
18 would be a competitive market, and again, the harm
19 should be measured in the context of ability to price
20 above competitive levels.
21 When deciding whether that conduct is
22 exclusionary, that is, giving rise to a Section 2 claim,
23 I believe that it is essential that deciding whether
24 there is substantial harm to the competitive process
25 must be undertaken first before any balancing against

1 any procompetitive justification, much as what Susan
2 said, it is very difficult for much of this conduct to
3 have a "procompetitive justification."
4 The concern from a principles standpoint is if
5 you quickly, say under a Microsoft type analysis,
6 shifted the burden for procompetitive justification and
7 there was none, you may end up penalizing under the
8 antitrust laws tortious conduct that does not
9 substantially harm the competitive process.
10 Finally, when a monopolist's exclusionary
11 conduct is subject to another regulatory scheme designed
12 to promote competition, the antitrust laws should
13 provide a remedy for such conduct only after taking into
14 account the structure of the market and the significance
15 of the regulatory scheme to the workings of the market.
16 This is going to be particularly important when we are
17 talking about Hatch-Waxman, as Preston was talking about
18 in the patent arena, or even one explanation for
19 Conwood, because we must remember that because there are
20 virtual bans on advertising, the conduct there was such
21 that it was difficult for Conwood to counteract the
22 activity because it could not do so by traditional
23 advertising in the regulatory scheme that we have with
24 respect to tobacco advertising prohibited that.
25 With that, let me now first go to abuse of the

1 government processes through deception, and the first,
2 of course, is Walker Process, and in the 41 or so years
3 since Walker Process was decided, much has been said
4 about Walker Process, and the issue with, of course,
5 Walker Process is that we start with the principle that
6 the patentee is immune from antitrust liability
7 generally when the patentee seeks to enforce its patent,
8 and so the question in Walker Process was, when would we
9 remove that immunity, and the Court said, well, when
10 there was fraud on the Patent Office, and if there was
11 fraud on the Patent Office, there was not then a per se
12 violation of the antitrust laws.
13 Indeed, when I read the opinion again, I believe
14 the Antitrust Division or -- I do not know whether the
15 Federal Trade Commission joined -- actually had urged
16 the per se rule, which the Court rejected there; that
17 is, that once fraud on the Patent Office is shown, the
18 plaintiff merely is now in the door and has to show
19 other -- an otherwise violation of the antitrust laws.
20 I believe the importance of Walker Process,
21 however, is Justice Harlan's concurrence, and in
22 particular, he wanted to make clear that this was not
23 going to open the door or should not open the door for
24 all sorts of plaintiffs' suits where a patent is found
25 to be unenforceable or otherwise invalid, and thus, he

1 concluded that the private antitrust remedy, which the
2 Court was allowing as a result of the Walker Process
3 case, should not be deemed available to reach Section 2
4 monopolies carried on under a nonfraudulently procured
5 patent.
6 Well, when we think about that sentence, I want
7 to remind you on a little bit of history. Noerr had
8 been decided prior to Walker Process, but California
9 Transport had not. California Transport comes six or
10 seven years after Walker Process, and so we end up in a
11 situation where -- and let me just sort of finish with
12 Walker Process for a moment -- that with Walker Process,
13 the standard is if you do have fraud on the Patent
14 Office, it is exclusionary conduct actionable under
15 Section 2 on the assumption that the patentee otherwise
16 possesses monopoly power or there is a dangerous
17 probability that the patentee will obtain monopoly
18 power.
19 One area where I would disagree with the Federal
20 Circuit, the Federal Circuit has said that in order to
21 bring a Walker Process case, there must have been
22 enforcement of the patent before the claim can be
23 brought. In my view, Walker Process, if there has been
24 fraud on the Patent Office, a Walker Process claim
25 should be available even if the monopolist patentee has

1 not attempted to enforce its patent. Now, I understand
2 that in virtually all circumstances, knowledge of the
3 claim and ability to bring the claim will be in the
4 context of either a counterclaim or where there has been
5 a cease and desist or some other letter, a declaratory
6 judgment action being brought, such that there has been
7 either actual or attempted enforcement. The difficulty
8 is that there are circumstances -- and this goes a
9 little bit to Preston's point, I believe -- where
10 someone will come and ask for a review of the current
11 patent law or current state of intellectual property, an
12 opinion by a law firm may be given to say, well, your
13 particular process will infringe. There is not
14 knowledge of the fraud on the Patent Office, and someone
15 who would otherwise come to market may not come to
16 market simply because that firm does not want to risk
17 the disruption of an enforcement action by the patentee
18 who has procured the patent by fraud. So, in my view,
19 the standard should not be one where Walker Process is
20 available only when there is enforcement.
21 Back to where I was going with Justice Harlan,
22 and the question becomes this, and something that I am
23 seeing in my practice, is where there is an allegation
24 that a patent is unenforceable by reason of inequitable
25 conduct before the Patent Office. Now, where there is

1 inequitable conduct, there is intent, there is
2 materiality, there is a weighing, but the basic issuance
3 of the patent is not in issue; that is, in a Walker
4 Process, where there is fraud, the patent is void ab
5 initio, where that is not the case with respect to
6 inequitable conduct. And here, in the Noble Pharma
7 case, the Federal Circuit distinguished between in the
8 case Walker Process fraud and inequitable conduct, and
9 the key for that distinction is in a Walker Process
10 fraud, there must be a fraud on the Patent Office, and
11 but for the fraud, the patent would not issue.
12 In my view -- and my time is getting short --
13 the problem is that where there is inequitable conduct,
14 there is often then a claim of sham litigation; that is,
15 that the litigation is brought with the patentee knowing
16 that its patent is unenforceable by reason of the
17 inequitable conduct. In my view, the standard there
18 should be one where the litigation must be sham, that
19 is, meeting the PRE test, and the sham litigation itself
20 must have substantially harmed the litigation; that is,
21 the focus of the inquiry should be on the sham
22 litigation and not the patentee's conduct before the
23 Patent Office.
24 Let me very quickly go to the issue of listings
25 on the Orange Book. The Orange Book, as many of you may

1 know, created under the Hatch-Waxman Act, a brand will
2 list those patents that cover the branded drugs which it
3 is marketing, and as we also know that the FDA plays
4 only a ministerial act, meaning it lists what is
5 presented to it.
6 One point that I want to make is that listing in
7 the Orange Book does have procompetitive attributes.
8 While listing in the Orange Book means that when a
9 generic sues, that there is a 30-month stay before the
10 generic can -- its ANDA can be approved by the FDA, it
11 also has a procompetitive attribute because it will
12 encourage the generics to sue because of the 180
13 exclusive for the first to file. So, we must be mindful
14 that listings in the Orange Book do have procompetitive
15 attributes, and where the FTC has sued in BristolMyers
16 and Biovale, in both of those circumstances, the
17 allegation was, in the case of BMS, it knew or could not
18 have reasonably believed that the listing was
19 appropriate or that Biovale was aware that the patent it
20 listed did not cover the drug that it marketed.
21 In Organon, I will pass through this, there is a
22 suit that said the court had no antitrust liability,
23 because Arganon had a reasonable basis for submission on
24 its patent in the Orange Book.
25 In my view, the standard should be that

1 something may be actionable exclusionary conduct under
2 Section 2 only when the decision to list the patent was
3 objectively baseless; that is, the test on whether to
4 list should be objective, and it should be looking to
5 where the brand could have reasonably believed that the
6 listed patent could be asserted against a generic that a
7 manufacturer would want to bring to the market.
8 Finally, on the tortious conduct, in my view, a
9 monopolist's misleading and deceptive tortious conduct
10 that's illegal in common law or another regulatory
11 scheme could be treated, may be treated, as
12 exclusionary, but only when the conduct is
13 institutional, pervasive and substantially harms the
14 competitive process.
15 Institutional, to me, goes to the question that
16 Preston raised of mistakes. This must be one where the
17 company has purposefully looked to undertake a campaign
18 that involves misleading and deceptive conduct. It must
19 be pervasive, that is, you measure it in the context of
20 the relevant geographic market. We have to, you know,
21 deal with the rogue employee who may be engaged in some
22 tortious conduct in some area, but we should not visit
23 antitrust liability.
24 It must impair the competitive process, and
25 finally, as has been suggested, in my view, there should

1 be no rebuttable de minimus presumption -- I know there
2 has been the suggestion in several -- I believe the
3 Sixth and the Ninth Circuits have adopted the notion of
4 a de minimus rebuttable presumption. I believe there
5 should not be one. The plaintiff in my view has the
6 initial burden, the initial burden being to present a
7 prima facie case of substantial harm to competition.
8 Thank you.
9 (Applause.)
10 MR. DAGEN: Our next speaker is Richard Rozek.
11 He is a senior vice president at NERA Economic
12 Consulting. After starting his career as an Assistant
13 Professor at the University of Pittsburgh, Richard
14 worked for over six years in the Bureau of Economics at
15 the Federal Trade Commission in a series of senior staff
16 positions, including Deputy Assistant Director for
17 Antitrust. Since joining NERA in 1987, Dr. Rozek has
18 worked on projects affecting many different industries,
19 including the pharmaceutical industry. His work has
20 appeared in a number of journals.
21 Richard?
22 DR. ROZEK: Well, I want to thank Pat
23 Schultheiss for inviting me to come here and talk today
24 about the pharmaceutical industry. It is an industry
25 that I spend a fair amount of my time studying, and the

1 work I do at NERA is focused on the pharmaceutical
2 industry as well as other industries, but I want to
3 begin by summarizing some of the interesting
4 characteristics or structural characteristics of the
5 industry that make it so interesting to study. Not only
6 that, we live in a world with laws regarding patents,
7 copyrights, trademarks and trade secrets that along with
8 the effective enforcement mechanisms have contributed
9 substantially to economic growth and development in the
10 United States. Nowhere is this effect of the
11 intellectual property laws more pronounced than in the
12 health care industry, specifically for pharmaceuticals.
13 Innovators in the pharmaceutical industry invest
14 hundreds of millions of dollars in research and
15 development or R&D for new medicines that address unmet
16 medical needs. Conducting R&D and obtaining approval
17 from the U.S. Food and Drug Administration or FDA to
18 sell a new medicine as a safe, effective treatment for a
19 particular disease usually requires 10 to 15 years of
20 research. Many research projects actually fail and do
21 not even result in the innovators submitting a new drug
22 application to the FDA.
23 For the few successful projects, the innovator
24 has, at the end of that 15-year period, a patent that
25 gives it exclusivity, not to be confused with monopoly

1 power, for components of the product. The patent may be
2 a composition of matter, may be a process, may be a
3 method of use. Also, the innovator has a new drug
4 application approved by the FDA as a result of that R&D
5 investment, but there is no guarantee that the product
6 will be commercially successful.
7 The innovator must manufacture and distribute
8 the product. The innovator must inform patients,
9 physicians, pharmacists, and payers about the
10 therapeutic benefits of the improved product. He must
11 negotiate prices with specific payers, both public and
12 private. And in the end, many pharmaceutical products
13 may not even generate sufficient revenues to justify
14 their investment. Those products that are successful
15 provide resources in terms of retained earnings for the
16 innovator to fund its ongoing R&D efforts. So that if
17 we want to have cures for such medical problems as AIDS,
18 Alzheimer's disease, and cancer in our lifetime, we must
19 have public policy that provides the incentives for
20 innovators to invest resources in pharmaceutical R&D and
21 continue the work to solve these unmet medical problems.
22 Now, there have been some concerns raised about
23 practices that innovators engage in near the end of the
24 patent lives for their products, such issues as filing a
25 Citizen's Petition with the FDA, introducing new,

1 improved versions of their products based on the
2 original chemicals, settling patent infringement cases,
3 introducing generic versions of their original branded
4 products, sometimes referred to as introducing an
5 authorized generic. These practices and others that we
6 have heard about today with regard to Orange Book
7 listings and so on, have been the focus of antitrust
8 scrutiny that the pharmaceutical industry has been
9 receiving.
10 This policy debate on whether or not these
11 practices are legitimate or the incentives to engage in
12 these practices somehow be altered are guided more by
13 emotion, rather than analyses that demonstrate that
14 there is actual harm to consumer welfare from these
15 practices. As a matter of fact, there are many
16 beneficial effects from these practices that often are
17 not the focus of the debate.
18 For example, filing a Citizen's Petition with
19 the FDA makes the FDA aware of scientific or public
20 health questions regarding its efforts to approve
21 additional products. Introducing a combination product
22 that combines two active ingredients or an extended
23 release product can actually provide benefits to
24 patients, increase compliance one pill instead of two.
25 Actually, for insured patients, it can result in lower

1 co-payments. You have to buy a single pill, pay one
2 co-payment, instead of take two pills and make two
3 co-payments, so there can be a cost-reducing benefit.
4 Settling a patent case can reduce litigation
5 costs and can actually, in some cases, provide
6 additional entry into a marketplace. Introducing an
7 authorized generic product into the marketplace can
8 obviously increase competition. So, you see that there
9 are benefits to the practices that have been the subject
10 of these challenges, and there appears, on the other
11 hand, to be a lack of evidence that these actions harm
12 consumers.
13 Instead of talking about these types of
14 actions collectively, I'll talk about the authorized
15 generic issue, which has been the subject of some
16 debate. There has actually been legislation proposed
17 addressing authorized generics. There have been some
18 court decisions related to authorized generics and so
19 on. Most recently, to spur the debate, the Supreme
20 Court refused to hear the FTC appeal of the
21 Schering-Plough case. The Court of Appeals for the
22 Second Circuit denied a consumer group's request for a
23 rehearing in the Tamoxifen matter that involved Astra
24 Zeneca and Barr settling a patent case. Bruce Downey,
25 the Chairman and CEO of Barr, said in response to the

1 Court of Appeals' decision, "We are pleased that our
2 patent challenge settlement related to Tamoxifen citrate
3 has been upheld as being pro-consumer and
4 pro-competition."
5 In spite of these court decisions and in spite
6 of the benefits to competition from introduction of an
7 authorized generic, the argument has been that
8 introducing an authorized generic is inconsistent with
9 the intent of the Drug Price Competition and Patent
10 Restoration Act of 1984, sometimes referred to as the
11 Hatch-Waxman Act. Specifically, the threat to launch an
12 authorized generic reduces the incentives provided to
13 generic companies to challenge patents listed in the
14 Orange Book and, thus, will reduce the number of future
15 generic alternatives.
16 Now, the problem is that there is no evidence
17 that the number of generic alternatives will be reduced
18 or that there are a lack of profit opportunities or
19 entry opportunities for generic firms. The Hatch-Waxman
20 Act actually encourages both innovation to solve those
21 unmet medical problems and competition or imitation by
22 sellers after patent expiration. It has generally been
23 a success because it has struck this balance between
24 innovation and imitation, and restricting options
25 available under the Hatch-Waxman Act to encourage

1 innovation, to destroy the incentives to develop new and
2 improved medicines, will actually harm patients,
3 physicians, pharmacists, and payers.
4 Now, some of the entry opportunities that
5 exist -- and this should be of interest to the antitrust
6 community as well, because it is an issue that is a key
7 part of any antitrust inquiry -- is what are the entry
8 conditions into a marketplace? Is entry encouraged or
9 discouraged by certain actions? Well, the presence of
10 authorized generics, for example, actually creates new
11 entrants into the pharmaceutical marketplace. Obviously
12 innovator companies now have an opportunity to introduce
13 an authorized generic and enter that component of the
14 industry, as companies such as Pfizer, Novartis and
15 Schering-Plough have done. Pfizer has its generic
16 entity, Greenstone, Novartis has its generic affiliate,
17 Sandoz, and Schering-Plough has Warrick. These are
18 firms that now sell generic products. So, innovator
19 companies are entering the generic marketplace.
20 Companies that have traditionally been in the
21 generic marketplace and have launched their own generic
22 products or independent generics have also been involved
23 in participating in the authorized generic portion of
24 the industry. Mylan, Barr, Par, Watson, Ivax/Teva,
25 which is now a single firm, have all sold authorized

1 generic forms of drugs under licenses from the innovator
2 varieties. Barr, a company that actually derives most
3 of its revenues from sales of generic drugs, has a few
4 branded products as well, and it recently launched an
5 authorized generic version of its brand oral
6 contraceptive product Seasonale after Watson, a generic
7 company, launched a generic version of the product.
8 Bruce Downey, again, said, quote, "It is our obligation
9 to preserve our rightful interest in this product." So,
10 you see, even the generic companies see the benefit of
11 launching authorized generics when they do expand into
12 the brand or innovator segment of the industry.
13 Some firms have arisen to sell authorized
14 generics only. For example, Prasco is a firm that
15 currently sells authorized generic versions of seven
16 branded products. It is a privately held company. It
17 was created because of the opportunities presented to
18 the marketplace by this ability to sell authorized
19 generic products.
20 I have seen various estimates of the value of
21 the patented products coming off patent in the next two
22 or three years, and it could easily exceed $27 billion
23 in 2007 and $29 billion in 2008. So, the point is that
24 there are profit opportunities in the generic industry
25 with authorized generics in the marketplace as well.

1 So, the new entrants have emerged, and future profit
2 opportunities exist.
3 The issue remains, however, what is the role for
4 antitrust policy versus competitive forces in this
5 industry? Where in the industry should antitrust policy
6 be focused? Should it be focused at the manufacturer
7 level? Should it be focused at the retail level?
8 Should it be focused at the distribution level? There
9 are fundamental questions with regard to using antitrust
10 policy to address issues in the pharmaceutical industry.
11 I think there have been several mistakes in the current
12 application of the antitrust laws to the pharmaceutical
13 industry, broadly defined as this vertical chain from
14 research through distribution of the products to
15 patients.
16 One is that market definitions are often too
17 narrow in this industry from an antitrust perspective.
18 Market definitions that use a single chemical as the
19 appropriate defining characteristic of a market,
20 overlook the therapeutic competition that exists in the
21 pharmaceutical industry, competition between chemical
22 entities, Avandia competes with Actos, Fosamax competes
23 with Actonel, ear tubes compete with antibiotics for
24 treating otitis media. There is a lot of competition
25 that's overlooked by taking the static view that it's

1 only a single chemical constitues a relevant market.
2 Well, a fundamental flaw in current antitrust, taking a
3 too narrow view of the market, not realizing the
4 therapeutic competition, competition across therapies,
5 be they pharmaceutical or surgical procedures.
6 Taking that narrow view of market definition
7 causes decisions to be made that monopolies exist when,
8 in fact, they do not, you see.
9 Another flaw is taking a static, as opposed to a
10 dynamic, view of the market when you have a market
11 environment characterized by high expenditures in R&D
12 and new products emerging from research being done
13 within U.S. laboratories, UK laboratories, Japanese
14 laboratories, and even in other countries, such as India
15 and Argentina and Brazil, countries that are developing
16 and have recently improved their protection for
17 intellectual property.
18 Competitive forces are working in health care
19 markets, and I think a greater reliance on allowing
20 these competitive forces to work as opposed to
21 intervening too early with antitrust enforcement is a
22 better solution for everyone concerned. What we need to
23 do is to convince consumers that shopping for
24 pharmaceutical products, such as they do for other
25 consumer goods, is a good idea. We have to induce more

1 of a shopping or a searching procedure for the lowest
2 pharmaceutical prices.
3 I recently conducted with one of my colleagues a
4 survey of pharmacies in Crystal City, Virginia to
5 purchase the product albuterol, which is an asthma
6 treatment. We found that in a narrow geographic region
7 within Crystal City, Virginia, the price of a canister
8 of albuterol ranged from $8.19 to $26.49. We found out
9 this information just by calling the pharmacy and asking
10 them how much a canister of albuterol would cost. There
11 is often a significant difference in price, which you
12 can find out by just calling before you even go to the
13 pharmacy with your prescription.
14 WalMart recently announced a pilot program to
15 sell generic pharmaceutical products for $4 a
16 prescription. K-Mart is offering a 90-day supply of a
17 prescription for $15. The market is responding to the
18 need to control health care costs.
19 So, in conclusion, I want to say that innovators
20 in the pharmaceutical industry obtain patents and
21 regulatory approval in the U.S. They are subject to the
22 general U.S. antitrust laws, as are all companies, and
23 additional specialized rules, such as the Hatch-Waxman
24 Act, that strikes a balance between innovation and
25 imitation. This structure creates the incentives for

1 both innovators and imitators to develop, manufacture
2 and sell their products. To preserve the gains from
3 both types of activities, public policy, including
4 antitrust, should focus on maintaining a business
5 environment that allows innovators and imitators the
6 most effective means to manage their product life cycles
7 under the existing system.
8 In the case of innovators introducing authorized
9 generics and the other activities I described earlier,
10 competition has increased and new entrants have emerged.
11 Patients have had access to established therapies and to
12 new therapies, and they have the mechanism in place to
13 assure that research will be done on therapies to meet
14 unmet medical needs in the future.
15 With regard to the pharmaceutical industry, a
16 reliance on competitive forces rather than a stepped-up
17 antitrust policy that has focused on static analysis
18 under narrow market definitions holds greater promise
19 for controlling health care costs in the future.
20 Thank you.
21 (Applause.)
22 MR. DAGEN: Before we proceed to our last two
23 speakers, we will take about a ten-minute break. When
24 we come back, we will hear from Gil Ohana and George
25 Cary and then go directly from their presentations into

1 our round table discussion. Thank you.
2 (A brief recess was taken.)
3 MR. DAGEN: Okay, welcome back, everybody. We
4 have two speakers remaining, and after their
5 presentations we will follow with the round table
6 discussion.
7 Gil Ohana is Director of Antitrust and
8 Competition for Cisco Systems, a leading manufacturer of
9 networking equipment for the internet. He writes and
10 speaks regularly on licensing, standard-setting, patent
11 pools and other subjects at the intersection of
12 antitrust and intellectual property law. Before joining
13 Cisco, Gil was a trial attorney at the Antitrust
14 Division of the U.S. Department of Justice, specializing
15 in antitrust issues in high technology industries.
16 Gil?
17 MR. OHANA: Thank you, Richard, and thanks to
18 the Justice Department and the FTC for the opportunity
19 to speak today.
20 Susan Creighton earlier used the term "network
21 industries." I am in the networking industry, and in
22 the networking industry, something the customers care
23 about a lot is that networking products work together
24 well and the way that we make sure they work together
25 well is largely by participation in standard-setting.

1 So, we're very proud of the leading role that we've
2 played in developing standards that many of you use
3 every day, whether or not you realize it. To give some
4 examples, 802.3, which is the ethernet standard; 802.11,
5 which is the WIFI standard; TCPIP, which is the basic
6 transmission control protocol on which the internet
7 runs.
8 We also sell every year billions of dollars of
9 products that implement a wide variety of industry
10 standards, so both from the standpoint of participation
11 in standards development, from the standpoint of
12 implementation of standards in commercial products, we
13 are passionately interested in a transparent standards
14 development process. What do I mean by that? I mean a
15 process that values intellectual property rights but
16 that also recognizes, as the Justice Department did in
17 the Vita letter, that the incorporation of a patent into
18 a standard may confer on that patent significant market
19 power and that, therefore, the decision to incorporate
20 the patent into a standard should be made knowingly with
21 access to the best information that is available at the
22 time.
23 The deceptive practices in standards
24 development, therefore, run contrary to our interests.
25 They reduce our incentives to participate in standards

1 development, and they reduce our confidence that the
2 products we ship will not infringe or that if they do
3 infringe that we will be able to address the
4 infringement with a payment of reasonable licensing
5 fees.
6 I'd like to preface my remarks with a quote from
7 Justice Brennan in the Allied Tube case that I am sure
8 many of you have seen before. Historically, the
9 antitrust scrutiny that Justice Brennan referred to was
10 really around Section 1. More recently, the FTC in
11 particular has brought a number of cases involving
12 Section 2 issues in standards development, as we all
13 know. What I'd like to talk about today is those cases
14 without getting deeply into the facts of any of them and
15 make a few points about them.
16 First of all, to suggest that despite the title
17 of today's discussion, when we talk about deception, we
18 really ought to be talking about exploitation and not
19 deception. Second, that if you situate deception in the
20 broader panoply of Section 2, you come up with some
21 interesting conclusions, and I think Susan touched on
22 these earlier, regarding whether the risk of
23 over-enforcement operates as strongly in the context of
24 deception in standards development cases as it does in
25 Section 2 cases more generally. And last, I'd like to

1 comment on, since I am here in an event hosted by the
2 Justice Department and the FTC, I'll abuse a privilege
3 of being here by talking about how I feel the agencies
4 can best address issues of deceptions in standards
5 development, and I'll give you a hint, it's not just
6 about bringing cases.
7 I won't spend long on this slide. Here are some
8 examples all drawn from recent FTC decisions or
9 investigations involving deception in standards
10 development, and as the cases suggest, there are a fair
11 number of fact patterns -- I didn't, for example, deal
12 with government standard-setting here, the Orange Book
13 cases, et cetera, but there are a fair number of fact
14 patterns just in classic tech industry standards
15 development.
16 So, to unite the theory, I thought about a kind
17 of way of defining the issue, which is that it is a
18 patentee's exploitation of monopoly power that results
19 from the success of a standard for which their patent is
20 essential, where that power is created by actions that
21 run contrary to the rules or shared expectations of the
22 participants in standards development.
23 I'd like to focus on two parts of that
24 definition. The first is exploitation of monopoly
25 power, and the second is resulting from the success of

1 the standard.

2 First of all, on exploitation of monopoly power,
3 it seems to me that the analytical weakness of just
4 focusing on deception is that you are really missing
5 what matters, which is not the deceptive act itself, but
6 the exploitation of the market power that that creates.
7 Let me offer an example, as they say, ripped from the
8 headlines, though it is a situation that people in the
9 networking industry are aware of, as I think are some
10 people in this building.

11 The hypothetical is, a patent holder discloses a
12 patent in patent standards development, it offers to
13 license the patent for fully paid up $1 royalty, give me
14 a buck, use all you want. The patent holder then sells
15 the patent to someone else. The buyer buys the patent
16 without knowledge of the prior licensing commitment,
17 let's assume. The buyer begins to assert the patent
18 against companies implementing the standard, which by
19 now has enjoyed a great deal of success, and you won't
20 be surprised to learn that the successor is asking for
21 more than a dollar. The rules of the standards
22 development organization at the time did not
23 specifically require that licensing commitments made in
24 the context of the standards development effort, in
25 fact, bound successors, but if you ask people who

1 participate in the standards development effort, that
2 would certainly be their expectation.
3 What was the deception here? Well, there really
4 wasn't any. The successor was quite up front about what
5 they were doing. The initial patent holder did not
6 deceive anyone, the successor did not deceive anyone, so
7 where is the deception? It seems to me that what you
8 are really focusing on here is the exploitation, and the
9 exploitation begins at the moment that the successor
10 becomes aware of the past licensing commitment and the
11 consensus within the standards development effort that,
12 in fact, it would bind the successor as well. At that
13 point, failure to withdraw the claim and seek only the
14 one dollar royalty is I guess deceptive conduct, though
15 it seems to me more to be exploitative conduct.
16 Now, note in this case, the deception and the
17 exploitation essentially merged into one in the matter
18 of the standpoint of timing. In cases like Rambus and
19 BroadCom, obviously there is a much longer time period
20 between when deception occurs and when the exercise of
21 monopoly power will occur, thereby exemplifying the
22 point that the two may be different, they may be the
23 same, but in any case, what you want to worry about is
24 the second, not the first.
25 Listening to some of the discussion this morning

1 made me think of another reason why you want to focus on
2 exploitation rather than deception. It is the question
3 of inadvertent deception. Deception may very well be
4 inadvertent, and it is particularly true in the
5 standard-setting context. Where the rules of standards
6 development organizations are not clear, people can make
7 innocent mistakes. Exploitation is never inadvertent.
8 Let's move on to the second phrase I'd like to
9 talk about, the phrase resulting from the success of the
10 standard. Here we come to a significant difference
11 between the FTC's series of standards cases and what
12 I'll call kind of classic Justice Department monopoly
13 maintenance cases, AT&T, IBM, Microsoft, all of which
14 involve durable monopoly power and raise the question
15 and the understandable concern that what you should
16 really be worried about is the risk of false positives,
17 because in those cases, you are dealing with a
18 successful company, and you have got to tease out, a
19 pretty difficult analytical task, tease out specific
20 exclusionary conduct from what made that company
21 successful as a general matter. That's not easy to do,
22 a risk that I am sure many of you have seen the Learned
23 Hand quote that captured this.
24 Now, the question I would like to pose is under
25 what circumstances can you be sure that the deceiver in

1 a standards deception case is or is not what Learned
2 Hand would call the successful competitor? It seems to
3 me that in deception cases, the conduct and market power
4 elements of monopolization may focus on different
5 subjects. In other words, you may be worried about or
6 you may be focusing on different actors. Certainly you
7 would be focusing on whether the act of deception was
8 anticompetitive and then whether it lacked business
9 justification, but you would also be focusing not on
10 whether the deceiver gained monopoly power through its
11 actions, but whether the standard gained monopoly power,
12 and the standard may have gained monopoly power for
13 reasons that have very little to do with the underlying
14 deception.
15 In that sense, the risk of over-enforcement is
16 lowest when, first of all, the undisclosed intellectual
17 property right was not core to the success of the
18 standard. It was, in other words, nice to have. Now,
19 this isn't an argument for counting patents. The fact
20 that the undisclosed patent was one patent out of fifty
21 or a hundred or a thousand should not be dispositive,
22 because all patents are not created equal, but the other
23 thing you should think about is, what were the rejected
24 substitutes? First of all, did they exist? Second,
25 were they close? And third, can you say with some

1 degree of assurance that they would have been selected
2 absent the deception?
3 Now, that may not be the easy inquiry, but it is
4 a whole lot easier than figuring out whether per
5 processor licensing was the source of Microsoft's
6 vertical monopoly in operating systems in 1984. It is a
7 whole lot easier than figuring out whether lease
8 practices were the reason that IBM enjoyed a leading
9 position in mainframes for quite so long.
10 First of all, the time period is very
11 compressed. In the facts of the Rambus case, the period
12 in which Rambus gained monopoly power through the
13 insertion of its patents in JEDEC and competitive
14 alternatives were distorted was a matter of months. You
15 knew what the alternatives were. You typically, because
16 standards development activities are ostensibly
17 documented, have a good set of evidence to look to to
18 figure out what the alternatives were, why they were
19 rejected. It seems like an easier exercise, and because
20 it is an easier exercise, the risk that you are going to
21 get it wrong it seems to me goes down.
22 Let's talk about moving on to the culture of
23 standards development. First of all, standards
24 development is not a lawyer-intensive process, which
25 goes back to the point I made earlier about the risk of

1 inadvertent nondisclosure or the risk of inadvertent
2 deception. In thinking about that, I go back to the
3 Rambus case and the FTC's description of standards
4 development as a cooperative effort in which the risk of
5 deception is therefore present. I would like to think
6 that that is right, but it raises an interesting
7 question and one that antitrust plays a role in.
8 The question is, how do we get there? And it is
9 not just an academic question for this audience. It is
10 a question in which antitrust does not necessarily come
11 with clean hands, not the Government, mind you, but the
12 private enforcement. Specifically, because of the
13 pervasive antitrust scrutiny of standards development
14 that Justice Brennan spoke about in Allied Tube and
15 particularly the imposition of vicarious liability on
16 standards development organizations in Hydrolevel,
17 standards organizations got very, very, very concerned
18 about antitrust liability.
19 They do not know much about it, but they know
20 enough to be frightened, which is kind of like what we
21 would feel if suddenly a brilliant men appeared at these
22 doors and told us we would be locked in this room until
23 we came up with the next standard for high speed
24 wireless data communications, and the way they responded
25 to that concern was by developing rules that

1 systematically discouraged the discussion of what seemed
2 like efficient things to talk about, cost, patent
3 validity, pricing, particularly in the context of input
4 pricing.
5 The standards development organizations, for
6 whom the cost of defending that antitrust case to a
7 motion of dismiss, let alone summary judgment, would
8 consume multiples of their annual budget, decided we are
9 not going there, and we are going to enforce these
10 rules. That led to the development of what I will call
11 a culture of standard-setting in which people can be
12 forgiven for not having asked what seem in retrospect to
13 be obvious questions, like, hey, I really like your
14 technology contribution, how much is it going to cost me
15 to practice that, and instead being satisfied with the
16 answer, well, it will be reasonable, and also questions
17 like, well, can you prove to me that that patent is
18 valid? How much do -- do you have patents?
19 These are questions that seem, again, pretty
20 basic from the standpoint of lawyers with the benefit of
21 reading cases in this area but that the rules of the
22 standards development organizations often prohibited
23 discussion of, which suggests a role for the agencies,
24 but not necessarily a litigation role. I don't want to
25 dismiss the litigation role, having been at Cisco during

1 the Rambus case and having talked to many engineers who
2 were following the coverage of the case in EE Times,
3 which is a leading semiconductor trade journal, which
4 had a full-time reporter, believe it or not, covering
5 the Rambus case.
6 It did provoke a lot of interest, and cases are
7 very useful from that standpoint, but beyond that, since
8 antitrust in some sense played a role in creating this
9 problem, it can also play a role, particularly the
10 agencies, in helping address the culture of standards
11 development by helping the agencies understand or the
12 participants in standards development understand what
13 they can and cannot do, and I would like to say that we
14 are off to a good start in that, particularly with
15 statements like Chairman Majoras' speech at Stanford
16 last year, the recent Vita letter, and also some
17 statements out of the European Union regarding this, but
18 more dialogue is needed and more help from the
19 enforcement organizations to figure out how far they can
20 go to defend themselves from these risks, to in some
21 sense change the culture, will nevertheless be
22 necessary.
23 Thank you.
24 (Applause.)
25 MR. DAGEN: Our final speaker during the

1 prepared presentations is George Cary. George is a
2 partner at the D.C. office of Cleary Gottlieb. Before
3 joining Cleary, George served as Deputy Director of the
4 FTC's Bureau of Competition. George also was a
5 principal contributor to the 1997 modification of the
6 1992 Federal Horizontal Merger Guidelines, which
7 incorporated consideration of efficiencies in merger
8 assessment. He is a frequent speaker and writer on
9 antitrust issues.
10 George?
11 MR. CARY: Thanks, Rick.
12 We seem to have started with some very broad
13 principles at the beginning, through Susan's comments,
14 and have now narrowed down through Gil's comments to a
15 specific analysis of the standard-setting process. I am
16 going to take it one level more narrowly, and I am going
17 to talk about implementation of specific rules within
18 the standard-setting context and whether violations of
19 those specific rules ought to be treated as an antitrust
20 issue, an issue of antitrust concern.
21 The particular provision that I am going to talk
22 about is so-called FRAND licensing commitments,
23 commitments by participants in the standard-setting
24 process to license their technology on fair, reasonable
25 and nondiscriminatory terms, and I am going to start by

1 laying out several premises that you have already heard
2 referenced this morning but which I believe apply in
3 this case as well.
4 First, standard-setting eliminates competition
5 among alternative technologies. Companies that
6 otherwise would be competing to promulgate proprietary
7 standards have now gotten together and eliminated that
8 competition by agreement. Antitrust, therefore, has a
9 stake in policing that standard-setting activity.
10 Second, when proprietary technology is made an
11 essential element of an industry standard, the owner of
12 that technology gains market power, exclusionary power,
13 beyond what is inherent in the patent itself. Prior to
14 the adoption of the standard, the company can exclude
15 others from practicing the particular innovation
16 incorporated in the patent. After inclusion in the
17 standard, if it is an essential patent, the patent
18 holder can exclude firms from practicing the standard
19 generally. That is a much broader grant of monopoly
20 power and one, again, where antitrust has a stake in how
21 it is exercised.
22 Third, the proposition that nondisclosure of
23 patents after lock-in as part of a standard has occurred
24 has been recognized as an antitrust concern. I think we
25 have had a couple of references to that recognition this

1 morning, the Rambus case, the UNOCAL case, the Dell
2 case, and other cases where the Commission and the
3 courts have recognized that if you fail to disclose a
4 patent, if you have a duty to disclose because you are
5 part of the standard-setting body, and if, as a result,
6 you have gained market power because the standard has
7 now incorporated that patent, that raises antitrust
8 concerns.
9 My premise here today is that if you accept
10 those three propositions, then it naturally follows that
11 you have to accept the proposition that violation of
12 commitments to particular terms that the standard body
13 sets in order to ensure that there is no hold-up after
14 lock-in and that there is no extension of a patent
15 monopoly to a monoply of the standard as a whole, also
16 must raise antitrust concerns. So, violations of other
17 rules designed to constrain exploitation of lock-in
18 raise similar competitive problems to failure to
19 disclose, and therefore, ought to be treated similarly
20 under the antitrust laws.
21 What is a FRAND commitment? A FRAND commitment
22 is an agreement to license on fair, reasonable and
23 nondiscriminatory terms as a condition for including the
24 intellectual property within the standard. The purpose
25 of this is to avoid hold-up, the same purpose as a

1 requirement that patents be disclosed, and an obligation
2 to disclose is ineffective if there is no recourse for
3 violation of the FRAND commitment. If one can simply
4 disclose, agree to license, and then fail to fulfill
5 that agreement, it raises the same competitive concern
6 as failure to disclose in the first instance.
7 What are the problems that FRAND is designed to
8 address? Before the standard is adopted, companies have
9 options. They can invent around patents. They can use
10 alternative patented technology. After the standard is
11 adopted, those wishing to practice the standard no
12 longer have options. They are locked into the use of
13 the standard, and having sunk significant investment in
14 standard-specific resources, it creates the potential
15 for monopoly rents, because their elasticity of demand
16 is now much more inelastic. They need to recover the
17 investments that they have made in that standard, and
18 they are going to be willing to pay a higher price for
19 the patented technology than they would have prior to
20 the adoption of the standard.
21 Second, FRAND is a commitment to a common
22 enterprise. Participating in the standard-setting body
23 is a commitment to the efficiency and the success of
24 that standard. That promise is that all participants in
25 the standard, many of whom contribute intellectual

1 property of one form or another, have committed to each
2 other as a matter of good faith and fair dealing to
3 impose a mutual restraint on their exploitation of the
4 market power created by that standard and a commitment
5 that they will not price their intellectual property at
6 such a level so as to make the standard itself
7 uncompetitive or inefficient.
8 FRAND is designed also to ensure competitive
9 markets downstream for products that are compliant with
10 the standard. To accomplish this, there is a
11 nondiscriminatory element to a FRAND commitment where a
12 holder of intellectual property promises not to use that
13 control to disadvantage its competitors in producing
14 parts, equipment, networks that are compliant with that
15 standard. These are the goals of the standard-setting
16 process in imposing FRAND, and these goals, I would
17 submit, inform us as to how to properly interpret FRAND
18 in the context of an antitrust enforcement.
19 My next premise is that FRAND is enforceable
20 under the antitrust laws under standard, conventional
21 Section 2 theory. The holder of a patent included in a
22 standard gains monopoly power. What is the definition
23 of monopoly power under the cases? It is the power to
24 exclude others from the marketplace and the power to
25 control prices. If you hold a patent, if the patent is

1 essential to practicing the standard, and if you refuse
2 to license that patent, you have effectively excluded
3 competition from within the standard. If you hold a
4 patent that is essential to practicing a standard and
5 you charge an exorbitant royalty to competitors who are
6 producing products compliant with the standard, you have
7 imposed costs on your rivals, and those costs have to be
8 passed onto consumers, and you have gained the power to
9 control prices in that downstream market. Both of those
10 things are the hallmarks of monopoly.
11 When does monopoly violate the antitrust laws?
12 It violates the antitrust laws where it is willfully
13 acquired; in other words, where it is not competition on
14 the merits, when the monopoly is not based on superior
15 products, business acumen or historical accident. A
16 willful violation of a FRAND commitment to license on
17 fair, reasonable and nondiscriminatory terms is,
18 therefore, monopolization. You have a monopoly by
19 virtue of the power to exclude and control prices.
20 Making a commitment to FRAND that you then renege upon
21 or do not follow through on is willful acquisition of
22 that market power, and therefore, the two would
23 constitute a violation of the Sherman Act with a
24 requisite showing of competitive effects.
25 Antitrust courts are competent to enforce FRAND

1 commitments. Now, there has been some discussion about
2 this, but again, the idea that you can have an antitrust
3 violation by virtue of violating the essential elements
4 of Section 2 with no antitrust recourse is one I think
5 we would generally reject, and I think Susan articulated
6 the principles of that very well. Some have argued that
7 FRAND should be enforceable only under contract law or
8 under tort law, but if it is a violation of the
9 antitrust laws by virtue of its effect on competition,
10 by virtue of its effect on consumers, then the public
11 should have standing under the antitrust law and
12 recourse to vindicate a violation of the Sherman Act.
13 Participants in the standard-setting process may not
14 have the requisite incentives, and in any event, there
15 is a separate injury to consumers and to the public by
16 virtue of the exploitation of market power that results
17 from this kind of conduct.
18 Finally, if a court is capable of determining
19 whether conduct violates FRAND in a contract or tort
20 case, there is no reason why, as a matter of judicial
21 administerability, it cannot do the same in an antitrust
22 case, and there is no reason under antitrust policy why
23 it should not do so.
24 I am now going to illustrate a couple of
25 examples of FRAND violations and talk about how one

1 might go about proving such a violation in an antitrust
2 case. The first is the most obvious, the extreme case
3 of a refusal to license. If you have agreed to license,
4 the standard has now incorporated your patent and you
5 refuse to license, you now have the capability of
6 monopolizing the market for standard-compliant parts and
7 equipment and networks. That, it seems to me, is a
8 clear violation of the FRAND commitment. It is also a
9 violation of antitrust law, because now you have created
10 a downstream monopoly.
11 Second, if you discriminate against competitors,
12 the "ND" part of the FRAND commitment, in
13 standard-compliant markets, again, you are taking your
14 monopoly on essential technology and you are extending
15 it to product markets for standards-compliant parts and
16 equipment. The hold-up potential is very real, and
17 antitrust law has recognized this kind of vertical
18 integration and abuse of monopoly in one market to gain
19 a monopoly in another in a variety of settings.
20 One example might be the case of a
21 rate-regulated utility vertically integrating into a
22 market where there is no such rate regulation and then
23 using its market power to expel other competitors from
24 that market, and once achieving a monopoly, charging
25 higher prices in the unregulated market to evade

1 regulation in the regulated market. This is a similar
2 kind of phenomenon where a company might agree to
3 license on fair and reasonable terms but through
4 discrimination that excludes competitors in compliant
5 markets gains the ability then to charge the monopoly
6 price in the compliant parts and equipment market.
7 Such discrimination also has an effect on future
8 innovation and competition, because often in these kinds
9 of markets, you find that the companies that are making
10 the compliant parts are learning about how the standard
11 works in ways that allow them to make improvements on
12 the technology in the standard, and in the next
13 generation of standardization, provide a competitive
14 alternative to the firm that provided the essential
15 technology in the first instance. Eliminating those
16 kinds of innovators and competitors cements the position
17 of the firm providing the technology in the first
18 generation and potentially permits them to succeed to a
19 monopoly in the second generation without making the
20 kinds of commitments that a standard-setting body might
21 otherwise require or by raising what they might be able
22 to charge as a fair and reasonable royalty in the second
23 round.
24 Again, discrimination is well known to antitrust
25 courts. Antitrust courts look at that in the context of

1 the Robinson-Patman Act, of the Sherman Act, of
2 discriminatory pricing, of predatory pricing. This is
3 not a foreign concept, and antitrust courts have
4 demonstrated an ability to administer these kinds of
5 rules.
6 What does fair and reasonable mean? Again, we
7 have to look at the underlying purposes of the
8 commitment that is being made in the light of the
9 antitrust principles that are being addressed here.
10 Fair and reasonable means a royalty that reflects the
11 competitive environment before lock-in. I think Gil
12 described it very well. It is the value of the
13 innovation separate and apart from the additional value
14 that that innovation takes on by virtue of its
15 incorporation in the standard and by virtue of the
16 lock-in created by the standard.
17 Second, fair and reasonable means a royalty that
18 is sufficient to allow the standard itself to be a
19 commercial success, so that you do not have a situation
20 where the royalties are so high that the standard is
21 debilitated, weakened, and is not able to provide the
22 efficiencies that the standard is designed to provide.
23 So, how would one determine a fair and
24 reasonable value? One would look at the alternatives
25 that were available to the standard-setting body before

1 the standard was adopted. One would compare how close
2 those alternatives are, and one would ascribe a value
3 based on the benefits that the chosen technology
4 provides over and above the other alternatives. You
5 then might adjust that royalty if you find yourself in a
6 situation where the cumulative royalty stack is so high
7 that it impedes the efficient adoption of the standard.
8 Again, antitrust courts routinely compare the
9 but-for competitive world with the observed market when
10 assessing constraints, and this is no different. In a
11 price-fixing case, you would look at the price set
12 through the illegal restraint. You would then, through
13 economic evidence, look at what the price would have
14 been in the but-for competitive world. You would look
15 at the comparison, and you would say the difference is
16 damages. Again, here, one might look at what options
17 were available to the standard-setting body, how close
18 those options were, what did the standard-setting body
19 at the time think about their alternatives, and how much
20 incremental value, separate and apart from the lock-in
21 value, did the accepted technology provide?
22 Determining the fair and reasonable royalty is
23 within the competence of courts and enforcement
24 agencies. Courts routinely determine in the context of
25 a patent infringement suit what would a reasonable

1 royalty have been. The courts have developed a
2 standard. The Georgia Pacific case lays out a whole
3 series of standards that might be used to do that.
4 There are industry benchmarks that could be looked at.
5 There are examples of the licensing of the same
6 technology in a context outside of the standard, what
7 kind of royalty did that patent attract where it did not
8 have the benefit of the standard?
9 A comparison of royalties charged in other
10 standards might also provide a benchmark, and a
11 comparison of the royalty charged in a competitive
12 market with no FRAND obligation might also be looked at.
13 So, courts have experience in assessing those kinds of
14 things. There is a body of case law that informs us,
15 there is an antitrust principle that gives us a
16 benchmark, and the courts are certainly capable of
17 analyzing those factors.
18 So, in conclusion, I would cite to you Justice
19 Ginburg's decision in the Cable and Wireless case that
20 was cited previously, and I would just quote from
21 Justice Ginsburg when he says, "Anticompetitive conduct
22 can come in too many different forms and is too
23 dependent upon context for any court or commentator ever
24 to have enumerated all of the varieties." It does no
25 good to shut one barn door and leave others open. It

1 does no good to say failure to disclose is an antitrust
2 violation, but disclosure with commitments that you then
3 refuse to implement cannot violate the antitrust laws.
4 The courts are capable of looking at the factual context
5 and coming to reasoned decisions about whether the
6 antitrust laws have been violated because of the
7 creation of market power and whether a particular
8 actor's conduct should be adjusted as a result of the
9 commitments they made.
10 Thank you.
11 (Applause.)
12 MR. DAGEN: And I think it is now time for a
13 little inter-panel discussion. Each panelist -- I think
14 we will probably go in the same order that we did the
15 presentations, if you have any comments that you want to
16 share addressing other panelists' presentations or
17 questions that you want to pose to other panelists, we
18 can try to keep track of them and either have them
19 addressed as part of this discussion or further on down
20 the line. We are thinking three to five minutes per
21 person, if you have got that amount to go through, and
22 we will see how it proceeds from there.
23 MS. CREIGHTON: I am not sure I have three to
24 five minutes of things, but I had just a few points, I
25 think one comment on what Preston had to say a couple on

1 what Gil had to say.
2 First, on Preston's observations, I found
3 intriguing his remark by the one lawyer who quoted that
4 he does his level best whenever he can to turn a
5 contract dispute into an antitrust claim. I would think
6 that typically, if people are in a contractual
7 relationship, that means that they are probably
8 somewhere in the vertical chain of supply, and so my
9 guess is that those antitrust claims that he is turning
10 his contract disputes into are a whole variety of what
11 we would view as sort of typical arguments about
12 vertical restrictions, and yet somehow we do not think
13 that that problem with turning contracts into antitrust
14 disputes means that we should invalidate all those types
15 of Section 2 claims sort of ex ante as somehow
16 invalidating them.
17 So, sort of returning to the point I had made
18 about we need to separate the question about problems we
19 have with private actions from the substantive antitrust
20 analysis, I guess I would pose as a broad experiment,
21 suppose we did away with private antitrust enforcement
22 just for the time being. In that circumstance, I would
23 be curious for those who have voiced concerns about
24 bringing -- for the Government to bring an antitrust
25 enforcement action in the context of -- I guess what I

1 would call opportunism. If the Government is satisfied
2 that that conduct has, in fact, caused durable market
3 power, why would we nonetheless still eschew government
4 enforcement to remedy it?
5 With respect to Gil's point about intent, I
6 had -- that was actually -- I think I share the concern
7 that he does and had mentioned that one of the things
8 that can be misleading, so to speak, about using
9 business torts as our sort of initial predicate act for
10 an antitrust claim is that we really are not about
11 intent and that what you are trying to get at with a
12 business tort is different from what we are driving at
13 with antitrust, and so some folks had mentioned about
14 inadvertent deception.
15 I guess what I have tended to think of as
16 deception, I have been tending to think of -- I will
17 misuse Mr. Williamson again -- I think he defined
18 opportunism as self-interest with guile, and so I think
19 understanding it in that context, if we have -- what we
20 are really concerned about in antitrust is self-interest
21 with guile that causes durable market power, and that is
22 really what we are talking about here, not some narrow
23 business tort that may or may not fit the particular
24 facts of what we are concerned with, which is consumer
25 harm created by such market power.

1 And then my final point, I wanted to amplify and
2 underscore a point that I thought Gil made quite well,
3 which was sort of going back to the causation question
4 that people have raised with Section 2 claims in this
5 area. I would agree with his point that it would seem
6 that many of our more traditional antitrust cases
7 actually do pose that causation problem more forcefully
8 than the kind of opportunism cases that we have been
9 focused on here. So, for example, in the cases that Gil
10 had identified, the Microsoft case, the AT&T case, the
11 IBM case, obviously untangling the effect of the
12 particular exclusionary acts is a challenge, but that
13 does not mean it is a challenge that we should forgo.
14 I would say, by contrast, in an Orange Book
15 case, if you conclude that there actually was a listing
16 that was made self-interestedly with guile and there was
17 a patent on it that automatically excluded competitors
18 from the market for 30 months where competition should
19 not have been excluded, the causation issue is pretty
20 straightforward. So, I would agree with Gil on that,
21 that sometimes the standard-setting cases, misuse of
22 government processes, the causation issue actually can
23 be quite straightforward.
24 That was it for my comments.
25 MR. DAGEN: Thank you.

1 DR. McAFEE: Thank you.
2 Let me actually echo something that Gil said,
3 which is that it would be useful for the agencies to
4 provide guidance to the standard-setting organizations.
5 In particular, the prohibition of talking about costs or
6 for that matter the prohibition of negotiating prices
7 for the use of patented technology in advance are
8 actually quite harmful in making good decisions. It is
9 as if you had to buy a car without knowing what the
10 prices are, and so the inability or the fear of
11 discussing what technologies will cost when implemented
12 in the standard is itself something that is designed to
13 procure standards inefficiently.
14 The second thing I want to say is that -- and
15 also in response to Gil -- is when you buy a bath robe,
16 it comes with a somewhat optimistic statement that one
17 size fits all. One of the things that you learn in
18 studying standard-setting organizations is that they
19 solve very different problems from each other, and they
20 make their decisions in a very different environment,
21 and I think one of the things that will be a challenge
22 for providing guidance to standard-setting organizations
23 is that they actually -- one size will not fit all very
24 well.
25 In particular, the amount of information that

1 they have available to them at the time that they make
2 decisions is often very different. I know JEDEC, in
3 particular, would discuss proposed standards, and then
4 the individuals would go back and work in their labs and
5 see whether or not the proposed standard was something
6 they could actually build themselves and what problems
7 needed to be solved in order to practice the tentative
8 standard. They very much were not necessarily on the
9 same page, nor did they want to get on the same page in
10 the sense that they did not want to reveal things that
11 they knew about the technology, because that would give
12 them a competitive edge. Giving advice about just what
13 they are allowed to do in such a circumstance where
14 standards are chosen, where how the standard is going to
15 be implemented is not yet even known, is going to be a
16 challenge.
17 And then finally, I have to agree with George
18 that it certainly is not a solution to say we can
19 practice a RAND -- if I make a promise that I will
20 satisfy a RAND, which there is another definition of
21 RAND, which is research and no development, which seems
22 appropriate in standard-setting organizations, but --
23 and then charge an exorbitant fee after the fact, after
24 the standard has been adopted, that is no solution at
25 all, and certainly the antitrust laws -- that is, I am

1 going to completely agree -- that certainly the
2 antitrust laws, if they cover the deceptive conduct,
3 must also cover the failure to provide a RAND or failure
4 to live up to the RAND assurance. I am less confident,
5 however, that the courts can actually effectively
6 interpret what is reasonable.
7 Thank you.
8 DR. BROCKMEYER: I would like to comment a
9 little bit on some of the remarks of Preston and
10 Richard.
11 First of all, with respect to the issue of
12 private enforcement, I do not believe that we should
13 eliminate private enforcement, and indeed, I think the
14 decisions of the court over the last 20 years or so have
15 made it much more difficult for the plaintiff to
16 proceed, and indeed, the argument of I guess last Monday
17 or so in the Twombley case could also have an effect on
18 private enforcement, albeit that case is a Section 1
19 case.
20 But I do want to touch on private enforcement in
21 that I believe private enforcement is one way to explain
22 the result in Conwood. While not knowing what U.S.
23 Tobacco's presentation was before the jury with respect
24 to the existence of monopoly power and accepting the
25 concession that it did have monopoly power that was in

1 the Sixth Circuit, when we think about the evidence that
2 was put forth and the reasonable juror sitting there,
3 hearing about a monopolist whose salespeople are running
4 around ripping out racks and throwing them in dumpsters
5 and various other types of conduct with respect to I
6 guess misleading information being provided or whatever,
7 in my view, the result in Conwood is not particularly
8 surprising given that it was in a private enforcement
9 setting.
10 Now the question becomes, well, do we want to
11 deter that? Well, I think one way to look at it, and
12 maybe this is Susan's point, is does the result in
13 Conwood somehow deter efficient conduct? Are we going
14 to deter throwing out racks or whatever or are we going
15 to -- whatever, and I think the end result is I do not
16 find Conwood to be a particularly surprising case, and I
17 think it can be explained in the context of private
18 antitrust enforcement and a reaction of juries to
19 evidence.
20 With respect to the pharmaceutical arena and
21 Hatch-Waxman and the regulatory scheme, Richard is
22 absolutely right. As I've mentioned in one of my
23 principles, I think we need to take into account the
24 structure of the industry and the regulation involved.
25 On the other hand, when there is deception, when there

1 is anticompetitive conduct that disrupts the balance
2 that is struck in Hatch-Waxman, then I think antitrust
3 has an appropriate role to play. Indeed, I would say
4 that the Commission's case against Bristol-Myers and the
5 deception that was involved with Bristol-Myers is a very
6 good example of where antitrust properly intervened in
7 this particular setting.
8 MR. DAGEN: Richard?
9 DR. ROZEK: Well, as an economist, I was struck
10 by the discussion this morning that raised questions of
11 measurement. Economists like to practice their craft
12 and measure things. It comes up a lot in the areas of
13 misleading and deceptive conduct. One area where it
14 comes up frequently is in the issue of false
15 advertising. How do you measure whether an ad is really
16 false? It could have on its face a false statement or
17 it could be perceived as conveying a certain message
18 that is inaccurate, and so economists can do surveys and
19 interpret that survey result.
20 But in some cases, it is much harder to measure
21 whether something is misleading or deceptive, and I
22 think back to some of the cases I have worked on where
23 in one situation, for example, an organization had
24 funded some scientific research; it was concerned about
25 the scientific and statistical merit of the research;

1 that is, the scientific protocol followed and the
2 statistical tools that were used to analyze the results
3 of that data.
4 So, the company raised legitimate questions, I
5 thought, as a reviewer of an academic article would
6 raise in commenting on the methodologies used to conduct
7 the research, but it was criticized for doing that and
8 for suggesting that the article not be published. To
9 avoid bad publicity, the company just paid a large
10 settlement. How to measure whether that was -- whether
11 their withholding publication -- or their request to
12 withhold publication of the article was really
13 misleading or whether there were legitimate scientific
14 questions that needed to be resolved before publication,
15 was a much more difficult issue.
16 That brings me to the question that was raised
17 earlier about private actions following on government
18 settlements. When someone settles a particular case
19 with the FTC or the Department of Justice, and they may
20 have done a calculation at that point that settling the
21 case was -- even if they could win, settling the case
22 was within that company's interest, was in their
23 interests to settle the case, but then they do not
24 always adequately factor in the private antitrust
25 actions that are going to follow and the damages that

1 are at issue in those private cases. So, they do not
2 take a complete picture of the damage calculation and
3 factor it in when they settle.
4 So, sometimes -- I have had cases like this,
5 too, where people come to us after two or three of the
6 private cases have gone forward and say, "we are just
7 tired of paying all this money. We are going to fight
8 this now." And I say, well, you know, you should have
9 fought it at the FTC or the Department of Justice,
10 because you could have a better case there on market
11 definition and on entry conditions and so on. In some
12 settlement discussions, the full impact of the private
13 cases are not factored into those calculations.
14 And then I was struck by George's comments on
15 the FRAND standards and what evidence is actually used
16 to determine whether a royalty rate is fair and
17 reasonable. I think the discussion of Georgia Pacific
18 factors borrowing from the patent literature, and the
19 wealth of information in the tax literature on applying
20 the arm's length standard to valuing intangible property
21 on transfers between affiliated companies such as a UK
22 research lab and an Irish manufacturing plant, that
23 would be very helpful to apply in the FRAND context.
24 Now, I was also struck by the discussions of
25 private cases and whether or not there should be a ban

1 on private antitrust actions. It seems to me that not
2 an outright ban, but maybe some reform in the process.
3 Again, speaking to some of the cases I have been
4 involved in from my own experience, there was no reason
5 that the brand name antitrust litigation should have
6 gone on as long as it did until Judge Kocoras made the
7 decision that it was meritless. All but four
8 pharmaceutical firms who were initially sued in that
9 case settled. That case went on too long, and there
10 should have been a process in place to make a decision
11 much faster. So, there are areas where there could be
12 reform in the private antitrust cases to at least render
13 decisions on frivolous cases much faster.
14 I was struck also by Preston's comments on
15 Canada because of the absence of private actions. I did
16 a study of health care reform in Canada and compared it
17 to health care reform initiatives in the United States.
18 One of the key differences between Canadians and
19 Americans -- residents of the United States that you see
20 is that in Canada, they have a much greater confidence
21 in the Government as a solver of problems, and so they
22 trust the Government to provide their health care and to
23 provide high-quality health care. Whereas in the United
24 States, I think we saw it with the Clinton Health Care
25 Reform Initiatives, there was a great deal of distrust

1 in the Government as a solver of problems and more the
2 Government as a creator of problems. So, there is a
3 fundamental difference in Canada and the U.S. just in
4 terms of how the residents in those countries interpret
5 the Government and government action.
6 I think part of the reason you do not see
7 private antitrust cases in Canada is that, "Well, the
8 Government will take care of it" is the solution. Those
9 are my comments.
10 MR. OHANA: I'll segue on the point that the
11 Government will take care of it. I wanted to pick up on
12 Preston's comment regarding one size fits all and the
13 role that I posited for antitrust agencies relative to
14 helping standards development organizations and their
15 participants understand what I will call the limits to
16 self-help to avoid deception.
17 I agree with Preston that one size does not fit
18 all. The point I was making maybe was a little bit
19 different. I am not positing a role for the agencies in
20 creating the uniform code of standards disclosure rules
21 or standards patent licensing rules. Far from it.
22 Standards organizations need, because of the variety
23 that Preston mentioned, a lot of freedom in that area.
24 I think, nevertheless, it is useful for the
25 agencies to do as the Antitrust Division did in the Vita

1 letter and as the European Commission did in the letter
2 they wrote ETSI in June of this year, to set out what
3 are the points that you cannot go past? For example, in
4 ETSI, the European Telecom Standards Institute, one of
5 the proposals was to essentially create a cap that at
6 the start of a standards development exercise, all
7 participants would agree that any IP disclosed would
8 essentially be under a cap of X percent, and even if you
9 had a very fundamental, very broad, very valuable
10 patent, you were in there with the rest of the patents
11 fighting for your share of X percent, and the European
12 Commission quite rightly said that that was problematic,
13 and it is that role that I see the agencies playing in
14 terms of limiting what is now the considerable desire of
15 standards development organizations to enact rules that
16 address this problem proactively ex ante rather than ex
17 post.
18 MR. CARY: Just a couple of observations.
19 First, I think that Preston's observations about the
20 costs of antitrust enforcement, the difficulties of
21 administerability and perverse incentives are all points
22 that we constantly have to keep in mind and keep guard
23 of in terms of how one interprets and applies the
24 antitrust laws. But having said that, I think those
25 comments also paint with too broad a brush, and maybe

1 one size fits all does not apply in that context either.
2 I would say that for those of you who have not
3 read it, and I am assuming that is not very many, the
4 "Cheap Exclusion" article that Susan authored with her
5 co-authors is a brilliant piece. The idea that one can
6 rationally set about determining where to apply
7 prosecutorial discretion in a systematic way in coming
8 up with arrays of combinations of anticompetitive
9 conduct where antitrust enforcement is likely to do as
10 little harm as possible, is a prototype for how to make
11 prosecutorial decisions going forward.
12 And using that framework and integrating the
13 points that Michael made, I would set up an array, and I
14 would say, for example, at one end of the deceptive
15 conduct that we have been talking about might be false
16 advertising or sham litigation. In sham litigation, you
17 have a built-in control: You have a judge. And if the
18 case is frivolous and has no reasonable basis,
19 presumably a judge would be easily in a position to get
20 rid of the case quickly and efficiently; and if the case
21 is more complicated so that he cannot get rid of it
22 quickly and efficiently; then perhaps that is correlated
23 with the idea that there is a reasonable basis to
24 litigate the claim, and it ought to go forward.
25 So, sham litigation as anticompetitive conduct

1 would seem to be one which has a built-in mechanism to
2 police it, and in addition, one where the
3 anticompetitive injury is likely to be small. Attorneys
4 are expensive, but relative to the sizes of most
5 business, paying an attorney is not likely to debilitate
6 you from competing.
7 At the other extreme would be the
8 standard-setting discussion that we have had where SSO's
9 create networks, durable market power is created through
10 lock-in, it is very, very difficult to change those
11 networks once they are established, and the
12 opportunities for exploitation of market power are
13 therefore significant.
14 In addition, you have got antitrust concerns in
15 participants establishing royalty rates pre-adoption of
16 the standard which, again, puts a premium on antitrust
17 enforcement after the fact if there is a pattern of
18 exploitation that a participant then engages in. Maybe
19 somewhere in between might be the Orange Book context
20 where there is an immediate anticompetitive effect from
21 bringing the litigation, separate and apart from the
22 standard sham litigation (where the anticompetitive
23 effect might flaw only as a result of paying attorneys'
24 fees). So that is a middle ground, in light of the fact
25 that you still have a judge who could dispense with the

1 case very quickly if it is truly a sham.
2 So, I do not think it is necessarily appropriate
3 to say that antitrust has no role in any of these areas
4 because of the possibility of an unintended consequence.
5 Instead, I think you can array these things and you can
6 apply antitrust where it is going to have the highest
7 likelihood of procompetitive impact and the lowest
8 possibility of making a mistake.
9 MR. DAGEN: Thank you.
10 Does anybody else have any comments they want to
11 share before we move into our rapid-fire questioning
12 period?
13 (No response.)
14 MR. DAGEN: Okay, we have some slides that I
15 think we will get to in a second with some propositions
16 and questions, but I think just since George went last,
17 I just had a question about one of the propositions he
18 just made.
19 So, in terms of your sham litigation, which you
20 put at one end, it sounds like it would be a very strong
21 presumption that there would be no sham litigation
22 monopolization claims, because it either gets disposed
23 of quickly, in which case there is no harm, or it lasts,
24 in which case it is not sham. So, is that --
25 MR. CARY: Oh, I do not know that I would use

1 the term "presumption," because that implies a legal
2 rule. I would say that as a matter of logic and maybe
3 some casual empiricism, that will tend to be the case,
4 and therefore, as a matter of prosecutorial discretion
5 or as a matter of the kind of scrutiny that a judge
6 might impose on such a case, it should be at the end
7 where the plaintiff might have to demonstrate a little
8 bit more in terms of context and effect than they might
9 in other contexts.
10 MR. DAGEN: Any views from the rest of the
11 panel?
12 DR. BROCKMEYER: I would like to make a quick
13 comment about Richard and what George just said about
14 mechanisms for quick disposal of cases. I am going to
15 point two cases out to you and Judge Schwarzer. Judge
16 Schwarzer attempted in the Northern District of
17 California to impose a screen -- and I will use the word
18 screening mechanism to shed cases quickly, limited
19 discovery, and in an effort to determine whether there
20 was merit to the claim. If there was not, dismissal,
21 and you move on, okay?
22 There are two cases of Judge Schwarzer's in that
23 period that went to the Supreme Court, and both were
24 reversed, Kodak and Hartford. Those both came from
25 Judge Schwarzer. So, while I recognize that, I do not

1 know how receptive the courts will be to that type of
2 procedure.
3 And so as a result, you are right, George, yes,
4 one way to say you can get rid of the sham litigation
5 quickly. Possibly not. It may depend on the judge.
6 MS. CREIGHTON: Maybe if I could just pick up on
7 George's idea, sort of to continue -- and I also thank
8 you for the kind remarks, George -- because I agree, I
9 think, that it is definitely not one size fits all when
10 we are looking at this kind of conduct. Some is much
11 more likely to arise in circumstances where there is a
12 likelihood of causing durable market power, and I
13 think -- and I would agree with George that at the other
14 end, deceptive marketing claims where you are talking
15 about -- particularly when it is sort of dueling claims
16 about products, I think Judge Easterbrook in Sanderson
17 versus Culligan cases correctly points out on the do no
18 harm end of things or sort of not trying to chill
19 procompetitive conduct.
20 I think the FTC for the last 20 or 30 years has
21 been a pretty aggressive proponent of the notion that
22 advertising is a good, and so this is one area where if
23 you allowed claims of any -- sort of I disagree with
24 that advertising, he said bad things about my product,
25 that is an antitrust claim, that kind of claim can chill

1 procompetitive conduct and that advertising is as much a
2 good for consumers as price competition. So, I
3 appreciate George's refinement of my analysis, and I
4 would agree with it.
5 MR. DAGEN: So, Hill, did you have anything you
6 wanted to talk about before we move on?
7 MR. WELLFORD: I have one question that several
8 people glanced over, and I think George maybe most
9 directly, so I will start there.
10 What does your point about incentives say about
11 the kind of remedies that we should look for to be
12 procompetitive or perhaps even prohibit as the FTC tried
13 to do in the Schering case, if you want to characterize
14 it that way? You said, you know, certain participants
15 in standard-setting organizations, for example, may not
16 have the incentive to correct the -- to challenge or
17 challenge the correct way. Perhaps some people who
18 claim to represent the public, which was your point,
19 some would have better incentives than others. Is there
20 anything to that that you would like to share?
21 MR. CARY: Well, yeah, let me back up a bit and
22 start from the beginning on it. You start with the
23 question, why shouldn't a violation of these kinds of
24 commitments be enforceable only in contract or tort? I
25 guess a wrinkle on that would be if it is remediable in

1 contract or tort, why bother with antitrust,
2 particularly when, overlaying Preston's presentation,
3 antitrust litigation can do harm?
4 I was attempting to answer that question by
5 saying that there is a harm that might extend beyond
6 those individuals that might have standing to bring a
7 contract claim or a fraud claim, that that harm is also
8 a harm to consumers, and that that harm ought to be
9 vindicated. So, for example, let's say you have someone
10 who is not part of the original standard-setting
11 proceeding; let's say that a particular state law of
12 contract limits the rights of third-party beneficiaries
13 to only those who are directly anticipated to be
14 beneficiaries; and therefore, a nonparticipant in
15 standard-setting would not qualify, they would not have
16 a contract claim directly. Nonetheless, there might be
17 a situation where a violation of the standard-setting
18 rules would cause competitive harm, and that individual,
19 without standing under contract, might be an appropriate
20 party to vindicate it.
21 A second example might be a state fraud statute
22 or a state common law rule of fraud which says if the
23 representation was not made to you, you have no standing
24 to vindicate the fraud. Again, if a misrepresentation
25 is made about patents, for example; if the

1 standard-setting body for one reason or another decides
2 not to pursue that, say, for example, the perpetrator of
3 that misrepresentation has now stacked the
4 standard-setting body with its own agents,
5 representatives, network of suppliers, allies; but there
6 is a hold-up in the sense that the failure to disclose
7 the patent was real, and now the patent is being
8 asserted, why wouldn't a member of the public who is
9 paying the bill for that violation of the
10 standard-setting body's rules have an opportunity to
11 bring an antitrust case, claiming the antitrust damage?
12 It is that kind of thing that I was referring
13 to, in saying that people with standing may not have the
14 incentives, and people without standing may have
15 suffered the consumer injury or the anticompetitive
16 harm.
17 MR. WELLFORD: Does it follow from your analysis
18 there that a member of the public should be limited to
19 remedies that benefit the public or the competitive
20 process as a whole as opposed to that particular person
21 who has brought the lawsuit, and is that done today or
22 can it be effectively done?
23 MR. CARY: I do not think that there is a
24 necessity, just because of the standard-setting context,
25 to revisit all of the rules of antitrust injury and

1 antitrust damages. So, for example, the courts have
2 established rules as to what consumers can recover. The
3 courts have established rules as to what competitors who
4 are the target of the anticompetitive activity might
5 recover.
6 Those rules do not need be any different in the
7 context of standard-setting than they would be in any
8 other monopolization case or price-fixing case or other
9 antitrust violation. I do believe that an antitrust
10 injury requirement is appropriate.
11 MR. OHANA: Just to comment, to pick up on
12 something George said, it is by no means universal in
13 standards development organizations' IPR policies that
14 any implementer of the standard is given explicitly the
15 right to sue to vindicate a disclosure or a
16 nondisclosure made to the standards development
17 organizations. In fact, it is extremely rare in my
18 experience that they actually explicitly say that. So,
19 you are going to be proceeding at that point under a
20 third-party beneficiary theory, and a third-party
21 beneficiary theory will vary a lot with state law. So,
22 in that sense I agree with George that it is entirely
23 possible that the contractual remedy will not exist.
24 MR. DAGEN: A couple of panelists I think
25 mentioned the notion that the regular false advertising

1 sort of claim would be on the lesser end of the
2 perspective. I wanted to try to juxtapose that with the
3 standard-setting discussion that you were having, which
4 was let's say you have a misrepresentation not about IP
5 but something else within the standard-setting
6 organization. There was a case involving Heary brothers
7 a long time ago where there was an allegation, I
8 believe, similar to an Allied Tube sort of thing with
9 packing except involving misrepresentations about an
10 alternative technology that was to be accepted or
11 proposed for an alternative within the SSO.
12 Where do you think that sort of
13 misrepresentation more or less similar to the false
14 advertising I think that you were talking about, where
15 would that fall, if you have any thoughts on that?
16 Anybody?
17 DR. McAFEE: Theoretically, it should not
18 actually make any difference. If I establish my
19 technology as the standard by claiming that the
20 alternative technology sets the atmosphere on fire and
21 burns up the earth, it is not -- and that is fraud --
22 that is not true, then it has had exactly the same
23 effect. On the other hand, it seems much less likely
24 that in reality you are going to be able to pull that
25 off, because by and large, the standard-setting

1 organizations are composed of people who know technology
2 pretty well, and so your ability to impugn alternative
3 technologies seems much more limited than your ability
4 to keep secret, for example, that you have patents.
5 MR. OHANA: There are cases, and I am thinking
6 of the Schachar case in the Seventh Circuit, where, if I
7 remember the case right, there was an allegation that
8 there was a misrepresentation made to a standards body,
9 and I think the response of the Seventh Circuit was that
10 the answer to bad speech is more correct speech, and I
11 would tend to agree with that. Those cases are not
12 going to impose a high risk of durable competitive harm
13 and therefore are unlikely to require the intervention
14 of antitrust agencies or courts.
15 MS. CREIGHTON: I thought the Commission was
16 right in Rambus in focusing on the ability of the
17 representation to be adequately -- both that its -- both
18 public and rebuttable, I guess, in the sense of I think
19 they were focused in particular on collaborative
20 ventures where there's less ability to ferret out people
21 where it might be making misrepresentations, but they
22 were trying, I think, to be getting at this point about
23 is it something that can be responded to with the
24 contrasting speech.
25 So, if I could change your hypothetical, for

1 example, suppose the misrepresentation was that each and
2 every member of the standard-setting organization was
3 voting based on sort of independent assessment of the
4 technology, but, in fact, I have gone around and paid
5 off everybody to vote my way, so there is a
6 representation that everyone is voting unilaterally,
7 and, in fact, that is not true. It has been stacked.
8 It seems to me like that misrepresentation poses
9 the same kind of difficult-to-get-at or ferret-out
10 problem that misrepresentations about IP do, but they
11 would be quite different from saying you should not use
12 that guy's technology because it is bad and that guy is
13 right there and he can counter.
14 MR. CARY: Having set up the continuum and
15 putting that kind of conduct at one end, now let me
16 retract just a little bit, because I do think that there
17 are environments where sowing confusion through false
18 representations can, in fact, be an antitrust violation.
19 I would not say that it does not exist, and I am
20 reminded of the good old days of pop-up windows where
21 people who were trying to create applications software
22 that ran on particular operating system platforms would
23 find that when somebody went to activate that
24 application program, a little screen would pop up
25 saying, "you are about to go into unchartered territory,

1 and we cannot guarantee that your computer will not blow
2 up if you press the button."
3 There are examples where that kind of activity
4 causes consumers, who are not expert technicians, to
5 worry about using alternative software which might, if
6 it were allowed to grow and expand, reduce an
7 application barrier to entry and result in more
8 competition to the operating system. I would not say
9 that as a matter of law one should not be allowed to
10 pursue those claims in a well-pled complaint and beyond
11 summary judgment if there are facts to be litigated
12 about whether that kind of activity does, in fact,
13 retard the growth of competing technologies.
14 DR. BROCKMEYER: Well, yeah, I want to agree
15 with what George just said, and we need to be a little
16 careful, because while I agree also with what Gil said,
17 that often false advertising or false statements may
18 well be -- again, continuing to use the scale here -- at
19 very much the low end of the scale, I do not believe we
20 should fall victim to even possibly absolutist language,
21 which one of the cases that we looked at was a Judge
22 Easterbrook decision involving Culligan, where he has a
23 fairly direct sentence that says commercial speech can
24 never be the basis of a Section 2 claim.
25 I believe that is wrong, and indeed, to go back

1 to the quotation from Judge Ginsburg that George read at
2 the end of his presentation I think has it right, which
3 is, yeah, we need to look at the context of the
4 circumstances where the commercial speech or the
5 misleading statements are made and then measure the
6 effect of that in the context of the market in which it
7 is made.
8 MR. OHANA: I would agree with that. I would
9 just point out that in the context of ETSI section
10 consensus-based broad participation standard-setting, it
11 seems to me that the likelihood that a disparaging
12 statement by the proponent of one technology about
13 another technology is very unlikely to have competitive
14 harm, because there are going to be a lot of other
15 participants who are going to be eagerly awaiting the
16 response from the proponent of the criticized
17 technology, and there is going to be a discussion of it,
18 and in that sense, I think the likelihood of competitive
19 harm is very low.
20 What I would point to in the example that George
21 gave, which actually I had to look at when I was at the
22 Antitrust Division, because I think it involved a
23 company in the Pacific Northwest and the Windows
24 operating system, is that what was very interesting
25 about that is that it was actually used only in the beta

1 of I think it was Windows 3 or Windows 3.1, and what was
2 sort of interesting is that Microsoft then pulled it
3 when they actually released the operating system.
4 The argument from the complainants was that the
5 damage had been done, because obviously the beta test
6 was distributed to a lot of kind of key influencers of
7 the technology industry who were then going to write
8 articles, create demand for the product, knowing that
9 DRDOS, at least according to Microsoft, cannot work.
10 That might be a context in which responsive speech may
11 not be effective, because it has to happen in a very
12 short time period in which a lot of demand is going to
13 be set in a product market that is very subject to
14 tipping, which I guess goes to Michael's point that the
15 underlying facts matter a lot.
16 MS. CREIGHTON: Another fact pattern that might
17 be worth throwing out there at some point would be in
18 the context of something that cannot be responded to
19 effectively potentially with responsive speech or at
20 least some party is vaporware, saying you have got your
21 product coming when, in fact, it is not. So, that is a
22 deceptive statement not readily correctable.
23 I think Preston and Richard probably know the
24 literature better than I do, but I think Farrell,
25 Sloaner and others have written some articles about at

1 least in tipping industries the potential for such
2 statements to have anticompetitive long-term effects.
3 DR. ROZEK: I think part of the discussion has
4 to involve the sophistication of the buyer. If you are
5 making statements to a buyer about a competing
6 technology, the buyer has to be able to assess those
7 statements. It may not be in every case that they can
8 do that instantaneously. It may be a statement about
9 reliability of the product after it is being used for
10 two years. You would not know if that statement is true
11 or false up front. You may have to spend a lot of money
12 to buy the machine, let's say a medical device, a
13 lithotripter, for example, something you have to spend a
14 lot of money, you would not know about the reliability
15 until after you spent the money, put it in place,
16 trained your workers and used it for a period of time.
17 Not all people can make those kinds of assessments.
18 So, I think underlying all of this in the
19 standard-setting process, in the false advertising
20 cases, you really have to conduct a rule of reason
21 analysis. You have to think about the sophistication of
22 the buyers and their ability to interpret the
23 information in a cost-effective way, without having to
24 make a purchase and wait two years or so to determine if
25 the machine is going to break down or be reliable, for

1 example.

2 DR. McAFEE: I agree with that completely. In

3 fact, standard-setting organizations are unlikely to be

4 a place where misleading statements of that kind are

5 going to last. They tend to have a smaller number of

6 very well-educated individuals, and it is more -- the

7 vaporware, in particular, which is usually a gimmick to

8 buy time while you try to develop a product so that

9 another product does not become a standard.

10 Microsoft made various promises about Windows CE

11 as a way of trying to prevent Palm from becoming a

12 standard, although in the end, Palm did become a

13 standard. It did not -- the vaporware promises were not

14 actually effective in that case. But there, that is a

15 much more likely thing. We will eventually support

16 this, just wait another few months, and that may be

17 enough to buy time to prevent a competitor from entering

18 the market.

19 MR. DAGEN: If we could maybe put up a few of

20 our propositions for discussion, first, slide number 2

21 states, "Merely because a particular practice might be

22 actionable under tort law does not preclude an action

23 under the antitrust laws as well."

24 I think this has been discussed a fair amount

25 today. Is there -- I heard a lot of consensus on this,

1 but I wanted to know if anybody had any views contrary
2 to that view or proposition.
3 MR. OHANA: I do not know if it is contrary, but
4 let me just offer what I hope is an exacerbation. If
5 you look at Trinko, one of the facts in Trinko is that
6 the conduct that Bell Atlantic was accused of was in
7 parallel the subject of an FCC regulatory proceeding
8 that resulted in the payment by Bell Atlantic of fines
9 to the FCC, and there is language in the opinion, if I
10 recall, that says that essentially where you have got a
11 regulatory system and the regulatory system is intended
12 to vindicate competition, the existence of the
13 regulatory system matters relative to the antitrust
14 analysis.
15 Then you get this quote from Conwood, and I will
16 not try to reconcile the two except to note that I think
17 there is a tension there.
18 MR. DAGEN: Well, given -- go ahead, Susan.
19 MS. CREIGHTON: Though I think maybe the way to
20 reconcile the tension was -- as I recall, Trinko said
21 where there is another comprehensive regulatory scheme
22 whose purpose is to promote competition --
23 MR. OHANA: Exactly.
24 MS. CREIGHTON: -- and that is a pretty
25 important difference.

1 MR. DAGEN: Go ahead.
2 MR. WELLFORD: We have already covered the law
3 of contract a little bit, but let me talk about the law
4 of fraud and maybe some other areas. These areas of --
5 is developed in the common law over a very long period
6 of time as the collective judgments of the courts, the
7 common law courts anyway, has been that there is some
8 necessity to apply heightened pleading standards or
9 specialized pleading standards to them.
10 For example, in the law of fraud, you have
11 Federal Rule 9 and 9(B), which is the rule of
12 specificity, the rule to require justifying reliance,
13 and the law of defamation or misleading statements about
14 individuals in that area. You have the Supreme Court's
15 New York Times recklessness standard for defamation.
16 Are we at all concerned that imposing Section 2
17 liability, which very clearly has regular pleading
18 standards, regular Rule 8, is at all going to be an
19 end-run around any of those established doctrines, and
20 does that indicate that either we may be off balance
21 with Section 2 liability or we should have Section 2
22 liability but apply some different pleading standards to
23 try to vindicate those same concerns?
24 DR. BROCKMEYER: Well, let me respond first, and
25 somebody can probably tell me I am dead wrong, but I

1 believe, for example, in Walker Process, if you plead a
2 Section 2 claim based on Walker Process, you are subject
3 to Rule 9, and so you are going to have to plead with
4 specificity, I think in the case of Walker Process and
5 maybe in the case also of inequitable conduct, such that
6 I really wonder whether Rule 9 is already coming into
7 play when you need the heightened pleading standard when
8 fraud is the predicate act for the Section 2 claim.
9 MR. CARY: I guess I would respond that the
10 typical kinds of requirements under Rule 9 are not
11 ordinarily the kind that will not be able to be met in
12 an antitrust case of this kind. I mean, it simply asks
13 you to identify the kinds of statements that were made
14 and to whom they were made, and so in the
15 standard-setting context, it would be a statement that
16 you would agree to license on FRAND terms, for example,
17 that you did not intend to comply with or that you
18 represented that there were not patents when, in fact,
19 after the fact, you revealed the patents. The so-called
20 heightened pleading requirement I do not think is all
21 that heightened in this context.
22 I think in terms of the recklessness element,
23 there might be some room for divergence for the reasons
24 that Gil described, that the thrust of the matter, the
25 crux of the matter in the antitrust case is the

1 exploitation of market power, not the niceties of the
2 precise statements that were made, and I think in the
3 standard-setting context, especially one where you are a
4 member of the body that is establishing the standard, I
5 do not think there is scope for recklessness and then
6 exploitation of the benefits of that recklessness after
7 the fact.
8 So, maybe there is a divergence there, and maybe
9 there is also a divergence with respect to those states
10 that have imposed a clear and convincing standard on
11 fraud allegations, which is by no means the majority of
12 states, but there are some.
13 Again, I would say that since the crux of the
14 matter is the exploitation rather than the deception
15 that a clear and convincing standard would not have a
16 place in an antitrust case, whereas it might if what you
17 are talking about is fraud.
18 MR. DAGEN: Slide 4.
19 Given what we have just talked about in terms of
20 the use or the nonpreclusive effect of the actions under
21 contract or tort compared to an antitrust case, I was
22 wondering if anybody had any thoughts about the issue
23 raised in Trinko about the cost of false positives. I
24 know Susan talked about it a little, I guess several
25 panelists talked about it a little, about it not being

1 as significant a concern with respect to
2 misrepresentations, but I was wondering if the panel had
3 any additional thoughts on that question.
4 DR. McAFEE: I think one issue that has been
5 brought up is that while it is true that we do not have
6 to worry about chilling misleading statements, that is,
7 we are pretty happy to chill as many misleading
8 statements as we can, it was also brought up that there
9 is a fair bit of confusion among engineers, in
10 particular, about just what the antitrust laws entail
11 and that the threat of antitrust actions actually scare
12 the engineers a lot, and I think maybe the middle ground
13 here is to provide fairly concrete guidance as to what
14 is allowed and what is not so that we reduce that,
15 because it would actually be somewhat of a disaster if
16 companies instead of joining standard-setting
17 organizations said, well, we are just going to have our
18 own standard, let them fight it out in the marketplace,
19 which guarantees that the standard that comes out is
20 proprietary.
21 We are actually quite happy, it is quite
22 procompetitive, to have standards that are practiced by
23 many companies; that is, common standards that are
24 practiced by many companies. If you thought about all
25 batteries -- think about your digital camera, which

1 probably has a proprietary battery. That is a much more
2 expensive proposition than if you have double A
3 batteries because of the standard associated and
4 multiple firms practicing it. So, we do not want to
5 actually have that harm the open standards, and, in
6 fact, we want to make sure that what we do with Section
7 2 is encouraging open standards, not discouraging it.
8 MS. CREIGHTON: I am probably just repeating
9 what I have said before. I think maybe the one area
10 where you would be concerned about false positives here
11 particularly would be chilling advertising unduly,
12 because that obviously is a positive. I agree with --
13 who was it -- Michael who made the comment that we are
14 probably not concerned with chilling having racks pulled
15 out of the shelves, you know, and we would not be unduly
16 concerned about chilling blowing up a competitor's
17 factory, and there is all kinds of conduct we probably
18 would not be too concerned about chilling.
19 I guess more generally, on the question of this
20 specter that is haunting Europe of sort of -- specter
21 haunting the United States of unduly broadening Section
22 2 liability, you know, it is not like we have got a huge
23 number of cases here we are talking about where people
24 have taken a fraud claim and then tried to turn it into
25 an antitrust claim. We have got a handful, and I am not

1 even sure that it is very likely that we would see very
2 many, because usually they have to have some kind of
3 fraudulent relationship, you have to have a relationship
4 of trust and confidence, and the circumstances in which
5 companies are going to be engaging in that kind of
6 relationship would seem to be relatively discrete.
7 So, I guess while I agree with the Trinko
8 statement in general, other than advertising, I am not
9 sure that I see a big issue with chilling.
10 MR. CARY: I guess that brings to mind one of
11 the points that Preston made previously about lawyers
12 wanting to convert contract cases into antitrust cases.
13 It seems to me that in this regard, when you are talking
14 about allegations that essentially sound in fraud,
15 taking that and converting it to an antitrust case is
16 not something you would do as a matter of course in any
17 event.
18 First, you would still have to prove the fraud,
19 maybe not to a clear and convincing element, but then
20 you would also have to prove the other elements of an
21 antitrust case, which just expands your burden, and a
22 fraud claim is suitable for punitive damages. So,
23 limiting yourself to treble damages when you could get
24 punitives in a fraud case, I am not so sure that that is
25 necessarily the inclination most plaintiffs' lawyers

1 would take.

2 I think what that points out, again, is that

3 there is a different role for the antitrust law than

4 there is for the private law of tort or the private law

5 of contract in this setting.

6 DR. BROCKMEYER: Yeah, I want to make a quick

7 comment about what Preston said about engineers not

8 understanding the antitrust laws, and over time it was

9 not engineers, it was someone else, some other

10 occupation who does not understand the antitrust laws,

11 and I am not particularly sympathetic with the engineers

12 in that setting in the sense that the antitrust laws are

13 obviously an important segment of our body of law, and

14 in the engineer's development of a product or technology

15 or whatever, the engineer has to come to an

16 understanding with the assistance of counsel or

17 otherwise, and we proceed. Antitrust obviously at times

18 maybe we think has gone off course, but hopefully we

19 bring it back on course. So, I must say, I am not

20 particularly sympathetic to engineers that are sitting

21 out there and worrying about the antitrust laws.

22 DR. McAFEE: All right, I am going to make the

23 counter case, because what we are asking engineers to do

24 in the standard-setting situation actually flirts with

25 directly violating the antitrust laws. So, that is to

1 say, we are asking competitors to get together and set a
2 standard that they are all going to practice. So, there
3 is a sense in which they are already exposed to risk,
4 and as a society, we do not like the alternative,
5 because the alternative is the companies never get
6 together, they each promote different standards that are
7 not compatible, and the market chooses one, much like is
8 happening with DVDs right now.
9 We have multiple standards. The market chooses
10 one of them -- actually, does not matter whether you
11 think about old DVDs where you had plus or minus R or
12 new DVDs where you have HD and Blu-ray. The market will
13 choose one that will be proprietary. That is bad for
14 society. We would be better off as a society if we have
15 a single standard that everyone agreed on, a useful
16 standard that all of the companies get to practice.
17 And so unlike other cases of antitrust law where
18 we said these are the laws, you have to obey them, here
19 we are asking firms to get together and do something,
20 which certainly there is a phrase, "tickles the dragon's
21 tail," and it certainly tickles the dragon's tail of
22 antitrust law automatically just because the competitors
23 are standing in the same room.
24 So, I would argue, then, that it is incumbent on
25 us as a society to actually give them instruction so

1 that they do not just say, well, we are just not going
2 to go down that road. We are going to stay in our own
3 labs and never meet, because those meetings do actually
4 result in standards that are good for society.
5 MR. OHANA: I agree with Preston. I would just
6 make the point that over-emphasis on antitrust risk and
7 the idea that in some sense standards development is so
8 fraught that engineers cannot ask probing questions
9 about whether technology is patented, how much it will
10 cost to practice, et cetera, creates the risk of
11 significant inefficiencies as well, and you have to find
12 a balance here between recognizing the potential for
13 Section 1 problems in standard-setting and facilitating
14 the risk of Section 2 problems.
15 DR. McAFEE: I want to make an unrelated remark
16 on something that Susan has said several times. She has
17 referred to advertising as a good. This is -- I would
18 say that it is actually an emerging consensus among
19 economists, but it is hardly something -- if you went
20 back 15 years and polled economists, you probably would
21 not find 50 percent agreeing with that, although that
22 number has grown dramatically, so it is actually -- and
23 sometimes it is very cutting edge for the FTC to be
24 promoting that as its view, is that advertising is
25 itself a good. Everyone understood that informative

1 advertising is a good, but advertising which is not
2 directly informative, some sort of brand positioning
3 advertising and that kind of thing, to view that as a
4 good is actually very -- looks to the future.
5 An example of this, I think perhaps the most
6 extreme example, is playground equipment. There are
7 playground equipment companies that actually advertise
8 that their rivals' products -- and they name them --
9 kill children. Now, this is advertising we would not
10 want to chill, whether it is -- well, if it is false
11 obviously we would like to chill it, but on the other
12 hand, you have got to have -- you have to view that as
13 sort of a risky ad, especially because there is a sense
14 in which all playground equipment kills children in the
15 sense that there is stuff that you can do that will kill
16 you if you fall off it, for example, not used as
17 directed. This is -- the advertising here -- so,
18 advertising in the playground equipment area is
19 particularly extreme, and it is actually worth going and
20 getting the brochures. It is a pretty entertaining
21 example.
22 MR. DAGEN: That actually reminds me of an FTC
23 consent that we had a few years ago which involved
24 bullet-proof vest manufacturers having an agreement not
25 to engage in any sort of comparative advertising, so

1 they -- don't tell them -- we won't tell them yours
2 fails if you don't tell them ours fails. Similar to the
3 playground equipment in terms of mortality rates, I
4 think.
5 MR. WELLFORD: Let me ask one question, which is
6 taking it outside the standard-setting context, which is
7 probably special, if misleading conduct is such an
8 anticompetitive problem, why is it so absolutely common
9 between rivals in industries? And two examples I'll
10 make, and then you can react -- anyone, I will throw
11 this to Susan first perhaps -- as to whether there would
12 be necessarily an anticompetitive problem raised.
13 One is competitors are attempting to discover
14 your trade secrets by aggressive but legal means, and
15 your response is to start putting out misinformation so
16 that they will not. That is an extremely common fact
17 pattern. Does that raise concerns if they are a
18 dominant competitor? Is that part of the rough and
19 tumble of competition?
20 The other is if you are a dominant maker of a
21 particular product, are you permitted to do what lots of
22 product makers do, Sony with the PS3 or any variety of
23 car makers have done this, put out fake test products in
24 the market and do fake tests with consumer groups in the
25 hopes that your rivals will find out about the fake

1 tests and then try to design towards that fake thing
2 when you have got something real?
3 If you are a dominant competitor, do either of
4 those raise concerns in the fact that they are common
5 does not necessarily make them okay, as we have seen in
6 the cartel area?
7 MS. CREIGHTON: I guess I am having a hard time
8 seeing how either would be likely to create and maintain
9 durable market power, which I hope I was clear about,
10 but I think that that really is the crux of -- the
11 question is, if we have inefficient conduct that we
12 believe causes durable market power, that is what we are
13 trying to get at, and so we are not -- and, in fact,
14 part of my point had been we are not trying to make
15 torts a predicate act for antitrust. In fact, that is
16 exactly the wrong way to think about it.
17 So, the fact that this is conduct that you may
18 or may not like or might or might not be good, unless I
19 could see some way in which it was likely to be creating
20 durable market power, I would not care from an antitrust
21 perspective.
22 MR. DAGEN: Just following up on Hill's question
23 then, the mere fact that it raises your rivals' costs in
24 this context would not be sufficient in your mind? They
25 are either going down the wrong path I think was -- Hill

1 was suggesting or they have to counter, take some
2 counter -- so it raises their costs in the short run
3 potentially.
4 DR. McAFEE: I would actually object to that as
5 being characterized as raising rivals' costs.
6 MR. DAGEN: Okay.
7 DR. McAFEE: The rivals who have actually chosen
8 to investigate whatever they investigate, putting out,
9 you know, memos that say we are investigating this, the
10 rivals are free not to follow that, and, in fact, that
11 is -- I would say generally, the rivals are the best
12 informed. The general public is much more likely to be
13 misled, which is usually damaging to the originator.
14 So, if Sony says, well, we are going to deliver this,
15 and then they do not, that is harmful to Sony, not so
16 much to Microsoft.
17 MR. DAGEN: Why don't we head to slide 3. I
18 think we have had a lot of discussion about a lot of
19 these topics, and that was the purpose of this panel.
20 So, slide 3, "The jury could have found that --" this is
21 from Conwood -- "that USTC maintained its monopoly power
22 by engaging in the challenged conduct," and I would like
23 to focus this on causation issues.
24 So, what kind of causal connection must be shown
25 between misleading conduct and the creation of or

1 preservation of monopoly power? I think it was -- well,
2 Michael or Gil, one of them talked about what you would
3 have to show, and we would like to consider that issue a
4 little more.
5 DR. BROCKMEYER: Well, let me go first. Yeah,
6 basically what I had said was that you would need to
7 show -- I used the word institutional, that is, getting
8 away from the mistakes or the rogue district manager or
9 whatever, that is, that it was a conscious decision that
10 was corporate policy.
11 Secondly, that it was pervasive, and I thought a
12 little bit about how I would measure pervasive, and I
13 think I would -- what I suggested on the slide is
14 relative to the relevant geographic market. So, the
15 question is how much was there.
16 And then finally, ultimately, that it harmed the
17 competitive process, that somehow, in the case of
18 Conwood, that the throwing away of the racks and so on
19 and so forth harmed the competitive process among
20 Conwood and U.S. Tobacco.
21 As I mentioned earlier, I think it is a classic
22 case of what happens when you have private litigation in
23 front of a jury in that I just think about it as myself,
24 as I am sitting here, I am a juror and not an antitrust
25 lawyer, and I sit there, and here I have got a

1 monopolist who is undertaking these acts.
2 Now, one key, of course, is I think you have to
3 distinguish -- and the judge has to instruct the jury in
4 a way to distinguish between what was deceptive or
5 misleading and what was procompetitive. For example,
6 responding to WalMart or whoever it was, the
7 competition, to have a rack, or even being the category
8 captain or whatever, you know, in and of itself, those
9 are not necessarily deceptive at all, and it is
10 important that the court, in instructing the jury,
11 allowed the jury to sort that out, and, in fact, would
12 have to.
13 So, to me, again, as I said earlier, I think
14 Conwood is just a classic case of a jury's reaction to
15 the evidence presented.
16 DR. McAFEE: This is also probably a good time
17 to remember that the antitrust laws are designed to
18 protect competition and not competitors and that that is
19 an easy mistake for a jury to make, because it is a
20 somewhat subtle distinction, but that deceptive act
21 should be viewed in that light, is does this actually
22 affect competition in the industry or does this affect
23 just one competitor in the industry.
24 MR. DAGEN: I think one of the allegations in
25 Conwood was that as category manager, they were

1 supplying false information about their sales and their
2 competitors' sales, and there was some talk about
3 whether the information maybe was in public information,
4 easily rebuttable.
5 Does anybody have any sense of where that sort
6 of conversation would occur, where on the line that
7 would be?
8 DR. BROCKMEYER: Well, one -- I hate to use this
9 word, but when I thought about that -- and I teach
10 Conwood in my antitrust class, okay, I like Conwood for
11 teaching students, and the word that comes to my mind --
12 I hate to use it -- is whether, in fact, U.S. Tobacco
13 took on I am going to say fiduciary responsibility when
14 it became the category captain to provide that
15 information. Yeah, the person from Kroeger or whatever
16 said, I made my own decision, and U.S. Tobacco was not
17 going to sway me, but the point being is that once U.S.
18 Tobacco took on those responsibilities, I think it had a
19 bit of a higher standard of conduct than it would
20 otherwise have as a competitor going in and pitching
21 information, because it had committed to Kroeger or
22 WalMart or whomever to provide information not only
23 about itself, but about the competition as well, in a
24 role different than being just a competitor in the
25 market.

1 MR. OHANA: Let me maybe disagree with that a
2 little bit having advised on category management issues
3 over time. You always tell your clients when they have
4 been appointed, annointed, category captain that they
5 should provide truthful information to the retailer, but
6 it seems to me that the retailer knows the biases of the
7 category captain, that it is going to design a planogram
8 that promotes its products, and if you think that the
9 incentives of the retailer in any way parallel the
10 consumer welfare, then the idea that the dominant
11 company that is appointed category captain has some kind
12 of special obligation to be truthful seems odd to me.
13 This is not the context like the ones the FTC
14 identified in the Rambus case where you are talking
15 about a cooperative enterprise. There is a fierce
16 competition for shelf space. Everybody knows what the
17 biases of category captain are, and if the competitors
18 ever feel that they are being discriminated against by
19 the behavior of the category captain filtered through
20 the retailer, they know Kroeger's phone number.
21 MR. DAGEN: In terms of causation, Judge
22 Easterbrook in Sanderson distinguishes cases from
23 Hydrolevel and says Hydrolevel had an enforcement
24 mechanism by virtue of codes being adopted based on the
25 conduct in the standard-setting organization, and he

1 says in Sanderson there is just basically speech. Does
2 there have to be an enforcement mechanism of some sort
3 in either government or standards or some other means
4 before the requisite causation can be shown in one of
5 these misrepresentation cases?
6 MS. CREIGHTON: I guess I'd say no and cite U.S.
7 v. Microsoft. In the diluted Java, for example, there
8 was no enforcement mechanism. It was cooperative in the
9 sense that the standard-setting process is cooperative,
10 but the representation was come build to Microsoft Java
11 because all the applications that you build will be
12 interoperable with Sun's Java, and people had no reason
13 to suspect that those representations were not true, so
14 they went ahead and built applications using Microsoft's
15 version of Java and then discovered that, lo and behold,
16 they had just collectively created a library of programs
17 that would only run on Microsoft. So, there was no
18 enforcement mechanism there that I can identify other
19 than the fact that it was a network market, but
20 nonetheless, I think that that decision -- that the
21 Justice Department was correct in pursuing that claim
22 and the D.C. Circuit in upholding it.
23 MR. CARY: It seems to me that the issue is
24 durability, not enforcement, and the question is from
25 what does that durability derive? Does it derive from

1 network effects, from existing monopoly and interfaces,
2 does it derive from enforceability, does it derive from
3 the incorporation of a standard? It could be any of
4 those.
5 MR. DAGEN: If we could go to slide 7, this
6 states, "The Federal Trade Commission may consider
7 public values beyond simply those enshrined in the
8 letter or encompassed in the spirit of the antitrust
9 laws." That is from Sperry and Hutchinson, 1972.
10 So, one of the questions that arises in
11 connection with this agency, the FTC, is whether Section
12 5 gives the Commission a different role to play in
13 policing deceptive conduct than Section 2 of the Sherman
14 Act.
15 DR. ROZEK: One of the most difficult things to
16 deal with is arbitrariness on the part of the antitrust
17 agencies or any regulatory agency. If it is going to be
18 difficult for both buyers and sellers to understand what
19 the policies are going to be or the enforcement
20 policies, just introducing some arbitrariness into the
21 process, then I think there is a social cost to that.
22 For example, one of the things that is very
23 helpful in terms of enforcement of the antitrust laws
24 are the Merger Guidelines. You have Guidelines that
25 tell you how the antitrust agencies are going to look at

1 these things, and they follow those Guidelines. They
2 have essentially become de facto the standard for doing
3 competition analyses even in private cases.
4 To the extent that there is a hidden agenda or
5 there is a hidden policy trying to be achieved, laws are
6 going to be applied in an arbitrary manner. I do not
7 think that does a service to buyers or sellers or to
8 firms or consumers.
9 MR. DAGEN: We talked a little bit about treble
10 damage actions. The other remedy often available is
11 injunctive relief. Would that influence the standard
12 that anyone would recommend as to what sort of conduct
13 might be actionable, whether there is simply injunctive
14 relief or whether there is treble damages also
15 available?
16 DR. BROCKMEYER: Is your question in the context
17 of Section 5 or generally?
18 MR. DAGEN: More generally.
19 DR. BROCKMEYER: Okay.
20 MR. OHANA: Bringing it back to the context of
21 Section 5, I have the blessing and curse, as does Susan,
22 of being a California admitted lawyer where we have the
23 experience of private actions for injunctive relief
24 under 17-200 recently, and I note this is a cautionary
25 tale, narrowed significantly by state ballot referendum,

1 and the pattern in those cases is that the fact that you
2 can only get an injunction and not money damages did not
3 inhibit the creativity of people in using that law for
4 some truly bizarre ends.
5 MR. DAGEN: Anybody else?
6 DR. McAFEE: There has been a little boom in
7 sending out cease and desist letters for spurious
8 copyright violations, for example. So, if I mention a
9 company's name and mention their product, they may send
10 me a cease and desist letter saying you are not allowed
11 to mention our name because it is a copyright or it is
12 trademarked, and that seems to be a case where something
13 beyond -- and these are not necessarily antitrust
14 issues, but agency action beyond the promote the First
15 Amendment, for example, might be called for, and so
16 insofar as other laws have a bearing on this, you might
17 want to be selective about enforcement or go beyond.
18 That is, I am going to agree, at least in principle,
19 that going beyond the letter of the antitrust laws might
20 be actually desirable in some circumstances, especially
21 as technologies move very rapidly.
22 MS. CREIGHTON: And just going back to your
23 Section 5 point, I guess I would say that I think
24 inefficient conduct that causes durable market power is
25 actionable under Section 2, is actionable under Section

1 5, and I do not think we need to extend or should extend
2 Section 5 to go beyond that to reach other kinds of
3 conduct.
4 MR. CARY: I guess I would slightly disagree
5 with Gil also as a California admitted lawyer.
6 MR. OHANA: Oh, sorry.
7 MR. CARY: I think it does make a difference
8 that 17-200 is limited to injunctive relief in terms of
9 what kind of damage it can cause to pursue the more
10 frivolous claims. I think the ability to get a motion
11 to dismiss on the damage claims granted, leaving only a
12 17-200 claim, is significant and to some degree I think
13 addresses some of the anticompetitive motives of
14 bringing antitrust litigation that Preston has
15 mentioned, and it leaves you in a position of simply
16 litigating before a judge and not a jury a novel theory,
17 which I do not think is quite so bad as facing the
18 barrel of treble damages.
19 MR. OHANA: This may be an area where the
20 perspective of inside and outside counsel may differ to
21 some degree. We do not enjoy 17-200 cases even though
22 there is no ultimate risk of damages because litigating
23 them is expensive, time-consuming and difficult, and
24 yes, it is somewhat better that there is no risk of
25 damages, let alone treble damages, at the end, but that

1 does not make the conversation with your general counsel
2 over how much you have spent on what is a completely
3 baseless action any easier.
4 MR. CARY: One man's cost is another man's
5 revenue.
6 MR. OHANA: I guess that's right.
7 MR. DAGEN: Turning to a variation on the
8 subject, are there any safe harbors in the area of
9 misleading or deceptive conduct that the panel would
10 suggest or panelists?
11 While you are pondering that, I will pose the
12 follow-up, which is what about in specific conduct
13 areas, the context of SSOs or false advertising or
14 patent abuse?
15 MR. CARY: I have got one example. I would go
16 back to the sham litigation example. It would seem to
17 me that if you are within Federal Rule of Civil
18 Procedure 11, which requires a reasonable basis for the
19 pleading, that being sued as an antitrust defendant for
20 sham litigation ought to be dismissed as a matter of
21 law. There ought to be a safe harbor if you have met
22 appropriate pleading standards. There should not be a
23 heightened standard for what might constitute sham
24 litigation.
25 DR. McAFEE: What if it is 200 sham litigations?

1 That is, it is not one, but we have sued 200
2 different -- so, I am thinking about the Recording
3 Industry Association of America. We have sued hundreds
4 of different defendants. So, we are doing it over and
5 over and over again. It is not clear to me that,
6 especially when it is against small defendants, that
7 there should be a safe harbor. I agree about one, but I
8 am not so sure I agree with many.
9 MR. CARY: Well, I think you are back to the
10 question of whether the lawsuit is reasonably calculated
11 to yield the result that you are seeking in the case or
12 whether it is calculated to reach some other result, and
13 I am not sure the number should make a difference if
14 each one of them independently would be deemed a
15 reasonable assertion of a copyright or a patent.
16 MR. OHANA: This is the first time anyone from
17 Silicon Valley defends the RIAA, but it seems to me if
18 they bring 200 cases against 200 accused copyright
19 infringers, those are all fair cases.
20 MS. CREIGHTON: I think what Preston is talking
21 about is the kind of case that would meet what is
22 referred to as the pattern exception to Noerr, where it
23 is filed without regard to whether it is true or not,
24 and so, you know, you are going to have a coin toss
25 chance of it being true or not, but -- actually I am

1 blanking on the name of the Second Circuit case where
2 they challenged each and every satellite certificate.
3 MR. CARY: Right.
4 MS. CREIGHTON: Primetime. So, it seems to me
5 that if you could satisfy the pattern exception in
6 Noerr, that would also stand up in antitrust law.
7 MR. CARY: Potentially it does under current law
8 in the Second Circuit and perhaps in the Ninth Circuit,
9 but I am questioning whether it should, especially in
10 the case of intellectual property where one of the
11 requirements for protecting the intellectual property is
12 that you have zealously protected that intellectual
13 property. The idea that then you could be charged with
14 an antitrust violation for having done what the patent
15 law requires you to do or the copyright law requires you
16 to do is problematic, and I think the key goes back to
17 your predicate, which is "without regard to the merits."
18 There is a distinction between bringing a case
19 which satisfies Rule 11, because you have a case that is
20 reasonably litigable on the one hand; and one that you
21 bring with no basis, which would violate Rule 11, in
22 which case if it has the requisite competitive effect,
23 there should be an antitrust remedy.
24 DR. BROCKMEYER: George, I need to give a small
25 refinement to your point, and I am not disagreeing with

1 you, but I am aware of circumstances where the initial
2 bringing of the suit met Rule 11, but during discovery,
3 it then, at that point during discovery, the plaintiff
4 learned that there was no basis for the suit such that
5 at that point then obviously if it pursues the case
6 after that, then I think there is an issue for sham
7 litigation. Now, whether that piece of litigation is
8 exclusionary, that I do not know, but I would not agree
9 that the safe harbor is, well, if you are okay at the
10 initial filing of the suit, you are okay, because,
11 again, of the circumstances I have discussed with you.
12 MR. CARY: Yeah, I think I recognize that
13 distinction, and I do not totally disagree with that. I
14 think it gets very complicated, though, because in that
15 context, now you are talking about work product and
16 attorney-client privileged communications, and it gets
17 very complicated to assess at what point you are
18 obligated to drop that kind of lawsuit.
19 DR. BROCKMEYER: Well, but the problem is in the
20 patent arena you may learn during discovery of the
21 fraud.
22 MR. CARY: Fair enough.
23 DR. BROCKMEYER: Okay?
24 MR. CARY: Yeah.
25 MS. CREIGHTON: I think I would probably

1 disagree with you, George, about the adequacy of Rule 11
2 sufficiently to guard against that anticompetitive
3 effect, because I think what you are proposing -- well,
4 usually my understanding of Rule 11 is an objective
5 standard, and so if you file every lawsuit and then it
6 turns out half of them are meritless, you get half of
7 them dismissed, but you have still raised rivals' costs,
8 and that is just sort of the willy-nilly filing, and to
9 your earlier point about a judge being able to serve as
10 an adequate gate-keeper, I do not think a judge
11 typically can serve as an adequate gate-keeper to that
12 kind of pattern of filing.
13 DR. McAFEE: Gemstar is alleged to be an example
14 of that.
15 MR. DAGEN: In terms of a kind of the safe
16 harbor, there is a Sixth Circuit case involving
17 podiatrists which looked at a multipart test and said to
18 survive summary judgment on a Section 2 case, you have
19 to show at least that there is a factual dispute, that
20 the statements were clearly false, and two, that they
21 were difficult or costly for plaintiff to counter. Is
22 that something that panelists would agree with?
23 DR. BROCKMEYER: Well, the problem with that
24 decision was that the Sixth Circuit adopted what I
25 indicated in my slides we should not have, which is

1 there was a rebuttable presumption, and George or
2 someone said this earlier, we are now getting somewhat
3 into procedural law. I do not think it is appropriate
4 to have the rebuttable presumption. So, in the first
5 instance, I would disagree with that case, and I think
6 they filed a Ninth Circuit case as well.
7 MR. DAGEN: Another statement in that case was
8 that there is no liability if the statements are simply
9 misleading as opposed -- and that court talks about
10 Matsushita and what we have talked about earlier with
11 Verizon and the danger of chilling procompetitive
12 conduct, and the Sixth Circuit is saying if it is simply
13 misleading, and I think they mean by that not
14 intentionally, if you cannot show from the beginning
15 that it was an intentional misrepresentation, but if it
16 is just a statement that turns out to mislead people,
17 then they would dismiss the case on those grounds.
18 MR. CARY: In the Walker Process context, that
19 kind of distinction is an important one. In patent
20 litigation, there is always something in the file,
21 especially if it is a complicated product deserving of a
22 patent, something in the file that one can point to as
23 being slightly irregular or perhaps not as articulate as
24 it might have been or using a term of art in a
25 particular way that is distinct from how some future

1 juror might interpret that.
2 Those kinds of technical issues that may or may
3 not give rise to inequitable conduct, it seems to me
4 that the judge does have an obligation to keep those
5 kind of, quote unquote, "simply misleading statements"
6 away from a jury and that some greater showing should be
7 required before a Walker Process fraud allegation could
8 be sustained.
9 MS. CREIGHTON: I guess I would repeat what I
10 have said before, which is I think the -- sort of the
11 intent element that seems implicit there maybe is a bit
12 misleading. I keep -- this analogy may be more
13 confusing than helpful, but I have tended to think of
14 like opportunism in contract. If a taxi driver picks me
15 up at the airport and says, you know, ten bucks, and
16 then pulls away and, you know, two miles later pulls
17 over to the side of the road and says, you know, I will
18 either let you out here or it will be a hundred bucks,
19 is probably not that relevant to me whether he thought
20 about that at the time he picked me up or only after we
21 left the airport, you know, it is still robbery.
22 And so in the same way, I do not know that it
23 would have mattered to my analysis if a Microsoft said,
24 go ahead and create, you know, applications using
25 Microsoft Java, it will interoperate, and at the time

1 the person said that, he meant it and was sincere, went
2 back home, and somebody said, well, actually, that is
3 not true, all these people are only going to be able to
4 write applications that work on our product, and he
5 said, oh, yeah, that is a pretty nice fact, why don't we
6 just keep that ourselves?
7 I am not sure that the intent at the time of the
8 statement is really -- for antitrust purposes, that may
9 sometimes be more confusing.
10 MR. CARY: Yes, I completely agree with that,
11 and I think this goes back to Gil's distinction between
12 exploitation and deception in the first instance. One
13 can imagine, for example, a scenario where someone in
14 good faith enters into a FRAND obligation, and then a
15 year later, the CEO changes, and there is pressure on
16 the stock, and he comes up with a brilliant idea, why
17 don't we just increase the royalties on these patents?
18 It would seem to me that that kind of exploitation is
19 just as much an antitrust violation as one with the
20 deceptive intent in the first instance.
21 MR. OHANA: And since we are in the world of
22 patent trolls and nonproducing entities, the fact
23 pattern that George just described is not one that is
24 unfamiliar to many of us where incentives change after a
25 patent is disclosed subject to a RAND obligation, and

1 what you thought was RAND based on what you perceived to
2 be the incentives of the party making the declaration
3 turns out to be quite wrong, often with significant
4 economic consequences.
5 At that point, I don't really care a whole lot
6 about whether the initial statement was made with guile
7 or opportunism. What I care about is the economic
8 consequence at the end.
9 DR. ROZEK: I think when you are talking about
10 safe harbor as being a more objective standard to apply,
11 like again, using the Merger Guidelines as an example,
12 with the Herfindahl Index standards in the Merger
13 Guideline. It is a more direct standard, easy to apply.
14 By contrast, whether something is misleading or not
15 misleading is difficult to determine with a bright line
16 rule. It would be harder in this context to have a safe
17 harbor as compared to the merger standard.
18 MR. DAGEN: Well, it is now approximately 1:00.
19 There are many other issues that we could have covered
20 today, but I think we have covered a lot of ground, and
21 I wanted to thank both the panelists and again the FTC
22 staff and DOJ staff who put pretty much all of this
23 together, and thank Hill. I would like to thank
24 everybody for being here, the panelists especially for
25 taking time out to educate us today, and I would like to

1 ask the audience to give one final round of applause.
2 (Applause.)
3 (Whereupon, at 1:02 p.m., the hearing was
4 concluded.)
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1 C E R T I F I C A T I O N O F R E P O R T E R.
2 DOCKET/FILE NUMBER: P062106
3 CASE TITLE: SECTION 2 HEARING
4 DATE: DECEMBER 6, 2006
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