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To: ATR-Agricultural Workshops
Subject: Comments Agriculture and Antitrust Enforcement Issues in Our 21st Century Economy

Legal Policy Section
Antitrust Division
U.S. Department of Justice
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Please see attached “comments.”

Regards,

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Gary W. Callahan

December 31, 2009

VIA E-MAIL

Legal Policy Section
Antitrust Division
U.S. Department of Justice
450 5th Street, NW, Suite 11700
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Re: Comments Regarding Agriculture and Antitrust Enforcement Issues
Restraints on Competition in Sales of Off-Patent Agrochemicals

I. INTRODUCTION

Over the last decade, the trend in the marketing of off-patent agrochemicals has increasingly been in favor of linking, or “bundling,” two different products together in a joint offering. Such product bundles are frequently justified as pro-competitive, because they have the immediate effect of lowering prices for one or more bundled products. On closer examination, such marketing strategies have the effect – and in fact may be designed – to foreclose competition. Such bundling strategies have come in two basic varieties which are discussed briefly in these comments.

The first type of bundle involves marketing programs combining the sale and planting of “genetically modified organisms” (“GMOs”) – i.e., seeds engineered to tolerate the application of one or more herbicides – and the herbicides that they are engineered to tolerate, which frequently are no longer patented. A company that sells or controls the sale (e.g., through licensing arrangements, supply agreements, or settlement agreements resulting from the application by a generic company for a registration under section 3(c)(1)(F) of the Federal Insecticide, Fungicide, and Rodenticide Act.) of both tolerant seeds and agrochemical herbicides can control the market for both through misuse of patents and restrictive grower agreements.

Upcoming product launches have been announced of crops that have been genetically modified to tolerate applications of agrochemicals that have been off-patent for decades, such as 2,4-D and Dicamba. Patents have been applied for and granted that would cover the use of such generic “staple” low-priced herbicides in conjunction with GMO crops. It is easy to imagine marketing scenarios that not only employ such patents to restrict the sources of these staple herbicides that can be applied to GMOs, but also effectively reduce competition in the markets for these herbicides on non-GMO crops as well.

The second type of bundle addressed in these comments is the “like product” bundle offered to agricultural chemicals distributors or dealers by multinational manufacturers. Such bundles involve two or more agrochemical products, one (or more) of which are under patent protection. Under such marketing approaches, the dealer or distributor, (and many times directly to large growers), is offered larger rebates or incentives for purchasing all of the bundled product lines and maintaining a minimum percentage of “loyalty” to the multinationals products, such as maintenance of geographical market

share, a minimum price, early order programs, and quantity of products sold. This, essentially, was the issue when DuPont Company sued Monsanto Company in the late 1990s for Sherman Act violations, when DuPont offered for free a competitive product to Monsanto's glyphosate.¹ However, some distributors would have lost income as a result of decreased bundle incentive payments from Monsanto by accepting the free DuPont product. Accordingly, they stayed with the Monsanto program.

Due to the substantial economic incentives involved in these bundling programs, a would-be competitor in one of the off-patent products covered by such a bundle has little or no chance to compete. For bundles that include patented products, competitors cannot offer a look-alike bundle without access to the patented product. New competitors can ill-afford to match the lucrative incentive payments offered by multinational companies. The result is a perpetual monopoly in the sale of off-patent agrochemicals by large multinationals.

In the antitrust workshops to be conducted during 2010, the USDA and the DOJ should make it a priority to consider the impact of such marketing and patent defense practices on competition in the markets for off-patent agrochemicals.

II. USE OF OFF-PATENT AGROCHEMICALS WITH GMO SEEDS.

Increasingly, agrochemical companies are obtaining patents to pesticide resistant/ tolerant crops. The claims of these patents often cover not only the GMO itself, but also the use of an off-patent agrochemical on the resistant commodity crops, such as soybeans, cotton, and corn. Although in such situations, according to established patent law, sales of the tolerant crop will "exhaust" the patent rights, the patent owner can nevertheless mandate or incentivize the purchase of the off-patent agrochemical through agreements with the growers. Even where the use of the patent-holder's own chemical product is not expressly mandated, creative marketing programs can be created that effectively limit choices for growers other than to utilize the agrochemical products offered or approved by the patent-holder.

Probably the most well-known examples of patents covering the use of off-patent agrochemicals on GMOs are the patents governing the use of the herbicide Glyphosate (the active ingredient in Roundup® brand herbicides) over-the-top of crops that have been genetically modified to tolerate the application of this herbicide. These patents have survived the expiration of the patent on the Glyphosate molecule itself; in fact, the first generation of such patents on commercialized varieties of GMO seed are not expected to expire until 2015.

However, this is not the only such example of patents covering the use of off-patent chemicals on GMO crops. Other herbicide tolerance traits on the market include imidazolinone tolerance and glufosinate tolerance. Tolerance traits are also frequently stacked with insect resistant traits, traits that

¹ Filed March 27, 2000. *SETTLED. CONFIDENTIAL*, April 3, 2002: Claim: Monsanto excludes competitors from selling glyphosate on Roundup ready cotton acres. 14.6 million acres of planted cotton in 1999. Monsanto has now sued DuPont to prevent it from producing Roundup herbicide-resistant corn and soybean seeds by combining Monsanto's genetic traits with its own. DuPont has counter claimed on an antitrust basis. See, *Monsanto Co. v. E.I. DuPont de Nemours & Co.*, 09cv686, U.S. District Court, Eastern District of Missouri (St. Louis).

improve the vitality of the crop plant, and other tolerance traits.

Upcoming product launches have been announced involving crops that have been genetically modified to tolerate applications of agrochemicals that have been off-patent for decades, such as 2,4-D and Dicamba. Patents have been applied for and granted that would cover the use of such “staple” herbicides in conjunction with GMO crops. At this time it is not known how the holders of the patents to such new GMOs intend to market such crops and whether such marketing approaches will include captive, licensed, or other limited “approved” sources of the agrochemicals which the GMOs are engineered to tolerate. However, it is easy to imagine marketing scenarios in which such patents are employed to restrict the sources of these staple herbicides that can be applied to GMOs, e.g. by means of a grower agreement, replant guarantees, etc.

Further, consider the impact of such restrictions on the larger market for the affected agrochemicals. A farmer may have been accustomed to purchasing supplies of 2,4-D and Dicamba from Company A for the last 10 years. Now, Company B offers a new patented GMO and also patents the use of 2,4-D and Dicamba over the top of such new GMO. Company B threatens to litigate against any one who infringes or induces the infringement of such use patents. The farmer is deterred from utilizing any other company’s supplies of 2,4-D and Dicamba in conjunction with the GMO crop. Further, the farmer does not need two suppliers of these staple agrochemicals and therefore confines ALL of its purchases of 2,4-D and Dicamba to Company B.

The ripple effects would not necessarily stop there, either. If Company A experiences an overall decline in its sales of 2,4-D and Dicamba, perhaps Company A leaves the market altogether. The marketing/patent defense approaches of Company B in connection with its new GMO thus have potential injurious effects throughout the market for 2,4-D and/or Dicamba.

Patents are legal monopolies over patented products. Patent owners have the right to sue for infringing sales of products covered by their patents. Patent monopolies are limited: patent rights are exhausted when the patented product is sold. *Quanta Computer, Inc. v. LG Electronics, Inc.*, 128 S. Ct. 2109, 2121 (2008) (citing *United States v. Unis Lens Co.*, 316 U.S. 241, 249 (1942)). **Patent exhaustion** has long applied to apparatus claims, but was not always extended to method claims. The Supreme Court in *Quanta Computer* held that method claims, like apparatus claims, “may be ‘embodied’ in a product, the sale of which exhausts patent rights” and that “[the Supreme Court] has repeatedly held that method patents were exhausted by the sale of an item that embodied the method” *Quanta Computer*, 128 S. Ct. 2109.

Relating to the patent exhaustion doctrine, “*Univis* teaches that the question is whether the product is ‘capable of use only in practicing the patent,’ not whether those uses are infringing.” *Quanta Computer*, 128 S. Ct. 2109 (quoting *Univis Lens*, 316 U.S. at 249 (1942)) (emphasis in original). *Univis* held that “the authorized sale of an article which is capable of use only in practicing the patent is relinquishment of the patent monopoly with respect to the article sold.” *Univis Lens*, 316 U.S. at 249. In *Univis*, the patent in question covered grinding lens blanks. The lens blanks had no other purpose other than to be ground into lenses. In *Quanta Computer*, the product sold was a microprocessor and the Supreme Court found no reasonable use other than incorporating them into computers that practice the asserted patents. Similarly, crops that are tolerant to agrochemicals have no other reasonable purpose than to be planted and treated with the agrochemicals to which they are tolerant. Following Supreme Court law, when a grower purchases a tolerant crop, the patent is exhausted as to the method of use with agrochemical.

As with patent exhaustion, **patent misuse** is an equitable defense against claims of infringement. *See, e.g., B. Braun Med. Inc. v. Abbott Lab.*, 124 F.3d 1419, 1428 (Fed. Cir. 1997). Patent misuse was designed "to restrain practices that did not in themselves violate any law, but that drew anticompetitive strength from the patent right, and thus were deemed to be contrary to public policy." *U.S. Philips Corp. v. Int'l Trade Comm'n*, 242 F.3d 1179, 1184 (Fed. Cir. 2005) (quoting *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F.2d 700, 704 (Fed. Cir. 1992)). Unlike patent exhaustion, patent misuse can also be the basis for an antitrust claim brought as a plaintiff's action. *See Senza-Gel v. Seiffhart*, 803 F.2d 661, 668 (Fed. Cir. 1986) (noting that patent misuse may serve, as here, as a defense to a charge of patent infringement but also as an element in a complaint charging antitrust violation). However, "[p]atent misuse may be found even where there is no antitrust violation, because '[p]atent misuse is . . . a broader wrong than [an] antitrust violation.'" *Id.* (quoting *C.R. Bard, Inc. v. M3 Sys., Inc.*, 157 F.3d 1340, 1372 (Fed. Cir. 1998)).

Tying arrangements fall under section 1 of the Sherman Act as anti-competitive behavior. Requiring a grower to purchase an off-patent, staple agrochemical with tolerant crops fits within the classic examples of tying arrangements. *See Leitch Mfg. Co. v. Barber Co.*, 302 U.S. 458 (1938) (the patent owner held a patent to a process of using a bituminous emulsion to cure concrete and tied sales of the emulsion to the process). More recent federal circuit decisions have discussed that when a patentee has market power and conditions a license upon the purchase of a separate, staple good, such practices are sufficiently anticompetitive so as to warrant condemnation on their face. *Va. Panel Corp. v. MAC Panel Co.*, 133 F.3d 860, 869 (Fed. Cir. 1997).

Although aggrieved competitors or consumers may resort to litigation on one or more of the above principles, it is the worst alternative for ensuring that competition continues to exist in the markets for off-patent agrochemicals. It is expensive, uncertain, and of long duration. Even in an anti-competitive environment, these factors are compelling deterrents to action by private individuals and companies. Rather, the agencies should utilize the forums created for the consideration of antitrust issues in agriculture to ensure that competition in agrochemicals is not injured by the development and commercialization of new GMOs.

Time is of the essence. Plans have been announced by Monsanto and by Dow AgroSciences for commercial launches within the next 1-5 years of GMOs that are tolerant to applications of 2,4-D and Dicamba, both of which are among the top 10 agrochemicals used in agriculture and have been off-patent for decades. Marketing plans for the GMO launches are no doubt in development as this is being written. It is imperative that the appropriate agencies review these impending product launches to ensure that competition in staple, off-patent products is not foreclosed or restricted to American farmers.

III. LIKE PRODUCT BUNDLING

Similar practices abound in the markets for sales of agrochemicals alone. A growing trend in the marketing of agrochemicals in the U.S. involves the creation of product "bundles" in which multinationals offer larger rebates to agrochemical dealers or distributors that buy a minimum percentage of their requirements for several chemicals from such multinationals. Although frequently justified as pro-competitive because they involve lower prices to the first-line customers for bundled products, such bundling programs have the immediate and long-term effect of keeping competitors out

and maintaining monopolies in the sale of off-patent chemicals.

The bundling of pyridine chemistry by Dow AgroSciences is one of the most notorious examples of this practice. Details of the pyridine bundling program are difficult to obtain due to confidentiality agreements and the reportedly severe consequences to a distributor or dealer who breaches such agreements, but it seems that the pyridine program works more or less as follows:

- a dealer or distributor (“customer”) is presented with a program to earn rebates or incentive payments (“rebate”) for purchasing pyridine products (Picloram, Clopyralid, Aminopyralid) from Dow;
- Picloram and Clopyralid are off-patent. Aminopyralid is still a patented product in the U.S. Therefore, no competing agrochemical supplier can offer a look-alike program that includes Aminopyralid without a license from Dow;
- A customer can buy one, two or all three products, but a customer that buys 2 products will have the opportunity to earn a bigger rebate than if it purchased 1, and a customer that buys all 3 products will similarly have the opportunity to earn a bigger rebate than if it purchases 2;
- The customer must purchase a minimum percentage of its requirements for each product from Dow in order to qualify for the maximum rebate. The minimum percentage is well above 90% and may be as high as 98% or 99%. The customer can buy less, but again, the rebate payments are reduced dramatically in the event the customer purchases less than the minimum percentage from Dow;
- Rebates are computed annually, and a portion of each payment is withheld and paid in subsequent years. If a customer in a subsequent year does not purchase the minimum percentage of all three products from Dow, it forfeits not only the rebate opportunity for such year but also a portion of the payment withheld from the prior year(s);
- Customers purchasing under this Dow bundling program will take into income, or book, the current year’s rebate payment, anticipate the following year’s payment of the total rebate, and repeat the same accounting practice going forward year to year; thus, once into the accounting booking of rebate income, the company can not effectively leave the bundling without the need for restating earnings for prior years;
- The bundling program was established in the years leading up to the expiration of the patents covering Picloram and Clopyralid. Thus, by the time competing suppliers of these now off-patent products arrived on the scene, customers were already enrolled in the bundling program, and carry-over rebate monies were already at stake. In short, new entrants had no opportunity at the outset to persuade customers not to enroll in the bundling program.

Clever marketing programs such as this (the above is one example of programs offered by multinational agrochemical companies) make it difficult or impossible for competitors in the bundled off-patent agrochemicals to compete. Customers are loathe to forfeit multi-million dollars of rebate payments to switch their business to a new entrant. The new entrants are unable to replace those lost dollars and still participate profitably in the business of selling the off-patent products. Further, part of those dollars are attributable to the sale of a patented product to which the new entrant does not have access and from which, therefore, it cannot earn revenues to defray the costs of making such payments to customers to entice them to switch. The result is a perpetual monopoly for the multinational in the sale of the off-patent agrochemicals in the bundle and permanent foreclosure of competition, to the detriment of choices and price competition at the farmer’s level.

In *Lepage's Incorporated v. 3M*, 324 F.3d 141 (3rd Cir. 2003), the majority of the Third Circuit

Court of Appeals upheld a jury verdict finding just such behavior to be anticompetitive. 3M had leveraged its multi-tiered product line in the private label market through rebates to customers who bought products in a number of 3M product lines. The majority found that the jury could have reasonably found that 3M exclusionary conduct cut its competitors off from key retail pipelines necessary for profitable competition. The court noted “[m]aintaining a monopoly is not the type of valid business reason that will excuse exclusionary conduct.” The type of conduct in which 3M engaged in *Lepage’s* is the same type of conduct observed with more frequency in the market for off-patent agrochemicals, with the same purpose of preserving a monopoly over an agrochemical.

The Third Circuit Court of Appeals further concluded that 3M’s exclusive dealing and bundled rebate programs violated Section 2 of the Sherman Act, and rejected 3M’s argument that selling above cost was a complete defense. Court observed: ***“The relevant inquiry is the anticompetitive effect of 3M’s exclusionary practices considered together ... The effect of 3M’s conduct in strengthening its monopoly position by destroying competition by LePage’s in second-tier tape is most apparent when 3M’s various activities are considered as a whole. The anticompetitive effect of 3M’s exclusive dealing arrangements, whether explicit or inferred, cannot be separated from the effect of its bundled rebates. 3M’s bundling of its product via its rebate programs reinforced the exclusionary effect of those programs.”*** “Substantial evidence [was shown] at trial that significant entry barriers prevent competitors from entering the tape market in the United States.”

The marketing conduct of some agrochemical companies in effect creates significant market barriers to entry by any competition. ***The result is de facto exclusivity.*** Discounts and incentives can produce this exclusivity — particularly where the entire dollar value of the discount is concentrated on the decision to buy incremental units. From the dealer buyer’s side, he faces a tax or “penalty” since he may lose all cumulative discounts. He has difficulty matching incentives since he has to match the absolute dollar value of the total discount on its own smaller sales volume and fewer products, necessitating a larger percentage discount. The unfortunate result is that a new entrant simply cannot compete, and the market for the bundled products remain perpetually exclusive to the multinational company offering the bundle.

IV. STIFLING COMPETITION

Beginning in the mid-1990s, Monsanto began purchasing companies in competition with its Glyphosate or seed businesses:

\$8 billion in seed company acquisitions of competitive companies since 1996:

Dekalb ECB resistant corn—glufosinate resistance; kills development of project
 Asgrow 1997 soy and corn
 Holdens 1997 corn
 Agracetes 1996
 Ecogen 1996
 Calgene 1997
 Plant Breeding International (Brazil) 1997
 Stoneville Seed 2005 cotton
 Delta and Pine Land Company 2006 cotton²

² Delta and Pine Land Company: largest producer of cottonseed in the US. DPL is the leading seller in the

V. CONCLUSION

The benefits of generic competition in agrochemicals are everywhere touted. For example, the price of generic Glyphosate has dropped dramatically in the last two years, in part to an increased supply; however, just as Glyphosate prices have dropped, Monsanto has increased the cost of its GMO seeds in a proportional amount. In short, those benefits should expand competitive alternatives and lower prices of inputs to farmers. Unfortunately, the marketing practices of multinational companies are either designed or have the effect of countering those benefits. Two such practices are described briefly above.

The upcoming antitrust workshops being conducted in 2010 by USDA and the DOJ are occasions for fruitful consideration of such practices, in order, among other things, to make these anticompetitive schemes transparent in the marketplace. The agencies should consider the impact of such practices on competition in the markets for off-patent agrochemicals. I believe that they will agree that such practices pose a danger to competition and should be addressed through regulatory or policy changes to ensure that farmers continue to have wide access to competitive alternatives in purchasing their agricultural chemical inputs.

Sincerely,

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MidSouth (MS, AK, LA, MO, TN). DPL sells 79% in MidSouth.
In Southeast (AL, GA, FL, SC, NC, VA) DPL sells 87% of all traited cottonseed.
In 1980s, Monsanto partnered with DPL to introduce Monsanto traits. This partnership has resulted in the introduction of “Bollgard” in 1996 and “Roundup Ready” cotton variety in 1997.
Farmers pay a price per bag to the seed distributor. The seed distributor pays the seed manufacturer for the seed and a separate license fee (“technology fee”) to the trait developer. Monsanto had earlier proposed to acquire DPL in 1998 and later abandoned the idea in 1999.