“Can you hear us now?” – Did the *Rambus* decision fall on deaf ears?[1]

A recent federal court decision on wireless ‘standard setting’ diverges from a previous FTC ruling, leaving some antitrust specialists perplexed. ***Richard Wolfram****, a solo antitrust practitioner in New York, explains why.*

Beyond the world of antitrust and intellectual property law, standard setting seems remote and arcane. Within it, though, it’s one of the hottest things going. Key principles of antitrust and IP come into play in standard setting – often in tension with one other – because, as competitors collaborate to forge common technological platforms (the two-prong plug, to take a simple example), they also seek to maintain control over their own proprietary rights.

As a matter of practice and statute, competing firms that participate in standard setting organizations (SSOs) are afforded some latitude by the antitrust laws to collaborate on standards. For such collaboration to achieve the desired goals, though, firms in SSOs must be able to rely on each other to deal fairly and in good faith, and to abide by the SSO’s rules. Opportunities for abuse, primarily in the form of deceptive conduct, arise more readily and can more easily be concealed in standard setting than in the “rough and tumble” of natural competition.

“The competitive risk [in SSOs],” explains one leading authority, “is that the misrepresentation will cause a standard-setting organization to adopt a standard it otherwise would have rejected, and that the adoption of that standard will in turn confer on the defendant market power it would not otherwise have obtained.” To safeguard against such abuse, SSO rules typically require participants to disclose any intellectual property rights that are essential to the standard, as it is being developed, and to agree to license any technology that becomes incorporated into the standard on fair, reasonable and non-discriminatory (FRAND) terms.

If abuse of the standard setting process is tolerated, firms will decline to participate and the promised efficiencies will fail to materialize – to the ultimate detriment of consumers. So, antitrust law has an important role to play in ensuring that the standard setting process itself is neither distorted nor hijacked through intentional abuse by any participant in the process. For this reason, monopolization law (based on deception as the predicate exclusionary conduct) is regularly applied in this context. The challenge for courts is to balance IP law and antitrust – on the one hand promoting proprietary technological innovation, on the other ensuring that the collaborative process of standard setting is conducted openly, transparently and without deliberate distortion.

Split decisions

Recently, two cases in particular have evaluated these issues – with radically divergent results. In early August, the Federal Trade Commission – which does not set precedent for the federal courts, but is viewed as authoritative in antitrust law and has significant enforcement and judicial expertise in standard setting – unanimously found Rambus Inc., a developer of technology for dynamic access random memory (DRAM), liable for monopolization through abuse of standard setting. Reversing the administrative court below, the FTC held that Rambus, in contravention of the disclosure rules and the reasonable expectations of the other members of the

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SSO, had deliberately failed to disclose intellectual property rights it had in DRAM technology which was then chosen to comprise a standard by an SSO in which it participated.

The FTC reasoned that Rambus had engaged in "patent ambush" through a course of dealing over several years in which it disregarded the SSO's disclosure obligations; deceived the other members; took advantage of their expectations; misled them to believe that it was not seeking patents that would be covered by standards decided on by the SSO; and even collected information about the pending standards and amended its relevant patent applications to ensure that subsequently issued patents would cover the ultimate standards. Recognizing both the procompetitive benefits and the potential for anticompetitive abuse in standard setting, and emphasizing the need for "procedures that prevent the standard-setting process from being biased by members with economic interests in stifling product competition," the FTC rejected Rambus's argument that its IP rights, including trade secret protection for its patent applications, trumped the SSO's rules.

Rambus had urged the FTC not to apply the balancing test of procompetitive efficiencies and anticompetitive harms outlined in *U.S. v. Microsoft,* but to apply instead the "profit sacrifice" test most recently applied by the Supreme Court in *Verizon v. Trinko* (which dealt with a claim of monopolization based on a unilateral refusal to deal). Under the profit sacrifice test, a monopolist's conduct is deemed exclusionary only if it would have been unprofitable for it to engage in the conduct but for an expectation that its conduct would exclude rivals and enable it to recoup its losses through the acquisition of long-run monopoly power. Rambus contended that its conduct was not exclusionary because it had no such expectation in keeping information about its patent applications secret and refusing to share that information with competitors. Rather, it said, its conduct was beneficial to itself regardless of what happened at the SSO or to its competitors.

The FTC reasoned that the profit sacrifice test is inappropriate when the conduct reduces consumer welfare but is inexpensive to execute, and so does not involve a significant profit sacrifice. Instead, it concluded, where conduct may have imposed substantial costs on rivals and contributed significantly to the creation of monopoly power, without reducing prices or causing the defendant to forgo sales or even spend substantial funds beyond what it otherwise would have spent (as happened in *Rambus*), the correct approach is to evaluate whether the monopolist's conduct on balance harms competition. (Rambus may appeal, after a decision by the FTC on remedies.)

If *Rambus* was unsurprising, it nonetheless brought some authoritative clarity to this area of the law. Yet, barely a month later, a federal district court in New Jersey appeared to set *Rambus* on its head. In *Broadcom v. Qualcomm* the court dismissed claims that Qualcomm, a cellular communications technology company, had violated the antitrust laws – in particular, Section 2 of the Sherman Act – when it reneged on its commitment to license on FRAND terms any technology that became incorporated into standards developed by the SSO in which it participated.

Factual differences aside, the two decisions are worlds apart, with some observers even saying that the *Qualcomm* decision would appear to make Section 2 monopolization law inapplicable to standard setting conduct. Although it would be a mistake to read too much into a single, unpublished district court decision on a motion to dismiss, *Qualcomm* has garnered significant attention and warrants further analysis, especially alongside *Rambus*. Furthermore, the decision appears to misapply the law. At the very least, it would be unwise to conclude from *Qualcomm* that, as a general proposition, an SSO member may renege on its commitment to license on FRAND terms in reliance on its IP rights or with relative impunity from the antitrust laws.

***Qualcomm* considered**

Qualcomm develops digital wireless communications products based on its so-called code division multiple access (CDMA) digital technology. Broadcom, a semiconductor supplier for wired and wireless communications, alleged that Qualcomm engaged in anticompetitive conduct in the markets for the technology and chipsets that operate cell phones employing wideband CDMA, a third generation technology implemented through a mobile telephone standard known as the universal Mobile Telephone System (UMTS). According to Broadcom (which asserts it needs a license from Qualcomm to compete with its UMTS chipsets), Qualcomm abused the procedures of international and US standard setting bodies by failing to license patents deemed essential to wideband CDMA technology and the UMTS standard, as required by the SSOs. The standard setting bodies adopted the UMTS standard in reliance on Qualcomm's written representation that it would license its patents on FRAND terms. (Broadcom and five other major telecom companies have also filed a complaint on similar grounds with the European Commission, which is expected to commence a formal investigation soon.)

Yet the district court dismissed without prejudice Broadcom's claims of monopolization, tying and exclusive dealing, and characterized the challenged conduct as "a refusal to deal fairly in the wideband CDMA market." Here, the court took its first tack away from *Rambus*. Rather than balancing alleged procompetitive efficiencies with anticompetitive harms under the *Microsoft* test, as the FTC did in *Rambus*, the court explicitly drew inspiration from *Trinko* on unilateral refusals to deal. If the right to refuse to deal with other companies is not unqualified, it noted, "the Supreme Court has nonetheless been very cautious in recognizing . . . exceptions because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single firm." On this authority, and in reliance on Qualcomm's broad IP rights as a patent owner, the court reasoned that "reviewing and supervising the terms upon which Qualcomm licenses its patents and offers to sell its UMTS chipset may be beyond the effective control of the court under the antitrust laws."

Yet the court had to address the specific conduct at hand, as alleged, and the framing of Broadcom's arguments in terms of monopoly power gained through abuse of standard setting. Despite its misgivings about applying antitrust law to Qualcomm's licensing terms, the court accepted that Qualcomm had reneged on its licensing commitment (and thus put aside for purposes of the motion the vexed question of what constitutes FRAND). It also recognized that Qualcomm's "alleged 'inducement' of the [SSO] may be considered anticompetitive conduct in the sense that a false promise biased the [SSO] in Qualcomm's favor, to the detriment of those patent-holders competing to have their patents incorporated into the standard." The court therefore accepted that the SSO had decided on the UMTS standard in reliance on Qualcomm's commitment to license its patents on FRAND terms.

And yet the court held that the false promise was not actionable under antitrust law, even if it may be actionable under another theory, such as breach of contract. Again, the court appears to have tacked sharply away from the FTC's reasoning in *Rambus*. In each case the defendant was deemed to have engaged in deception – either by failing to make the necessary disclosure (*Rambus*) or by falsely inducing the other participants to rely on, and failing to fulfill, its licensing commitment (*Qualcomm*). The FTC found that Rambus's deceptive conduct distorted the standard setting process and enabled it to monopolize the relevant markets by locking in its competitors to a standard which it then controlled through its patents. In *Qualcomm*, the court similarly found that Qualcomm had falsely induced other members of the SSO to choose its technology as the standard in reliance on its licensing commitment. When it became clear that Qualcomm would not honor its commitment, the industry could not turn back; it was locked in to technology Qualcomm controlled and which made it a monopolist in the relevant market *precisely because* the industry had chosen UMTS as the standard in reliance on Qualcomm's false commitments.

The question arises: why did Qualcomm's deceptive manipulation of the SSO's choice fail to amount to illegal acquisition of monopoly power? According to the rather obscure reasoning of the court, the answer is simple: the loss or preclusion of competition in the wideband CDMA market was not because of Qualcomm's false inducement, but because the choice of *some* standard inevitably results in the loss of competition. That is, it was the choice of a standard, not Qualcomm's conduct, that resulted in the loss of competition, in the view of the court. Yet this reasoning fails to address the consequences of an alleged breach of a licensing commitment. Indeed, it ignores the difference between competition on the merits (albeit in the scheme devised by an SSO) and competition that has been distorted through deception in a collaborative setting. As the FTC said in *Rambus*: "We cannot stress too strongly the importance we place on the fact that the challenged conduct occurred in the context of a standard-setting process in which members expected each other to act cooperatively."

Where now?

Accepting the reasoning of the *Qualcomm* court means accepting that the elimination of competition that inevitably results from the choice of a standard – whatever standard – somehow inoculates from antitrust scrutiny a member's willful distortion of standard setting that has induced other SSO members to select its particular technology as the standard. The fact that competition will inevitably be lost due to a fair selection of a standard does not excuse a loss of competition due to a distortion of the standard setting process, any more than a loss of competition through competition on the merits would excuse a loss of competition through illegal monopolization. It goes without saying that competition will be lost when a standard is chosen. But surely that doesn't preclude the application of antitrust law. The harm to competition that is the focus of antitrust law in these circumstances concerns the integrity of the selection process for the standard, not the loss of competition that naturally results from the choice of a standard. The *Qualcomm* court looked through the wrong end of the glass, and misconceived the "harm to competition" at issue in standard setting.

As a corollary to this misconception, and to its reliance on *Trinko,* the court also appears to have read too much into IP rights in the context of SSOs that impose disclosure and licensing restrictions as a condition of participation. The court is clearly correct when it says that "Qualcomm's 'power' to control the licensing of its patents is derived from the rights it enjoys as a patent-holder." After all, a patentee is statutorily entitled to license on terms of its choosing, or to refuse to license altogether. But the court paints with too broad a brush when it goes on to say that "[t]he adoption of an industry standard neither diminishes nor augments this exclusionary right," for the right is qualified when the patentee submits to a licensing commitment as a condition of its participation in an SSO.

Still, might the approaches of the FTC in *Rambus* and the district court in *Qualcomm* be reconciled? Is there a fundamental difference between an SSO participant's reneging on its commitment to license on FRAND terms and its non-disclosure of relevant IP, in contravention of the SSO rules and common law principles, which justifies the difference of approaches in these two cases? Does the court have a point here when it says that "[i]t is not the judicial role to re-adjust the risk in high-stakes commercial dealings"?

The answer is no, by these lights. It is hard to see on what grounds the court could say that its "no harm to competition" analysis for standard setting (i.e., that there was no harm because standard setting inevitably results in a loss or the elimination of competition) should *not* equally apply in *Rambus*, considering that in both cases the SSO participants were deceptively induced to select the defendant's technology as the standard. And if that logic were applied in *Rambus*, it would then be difficult to see how Rambus's deceptive conduct could be deemed exclusionary. The result would be that firms such as Rambus would be free to abuse the standard setting process at will – and standard setting would quickly be undermined. This is neither logical under the antitrust laws nor an acceptable policy outcome.

Broadcom, meanwhile, has appealed the decision, which it believes is "directly at odds with established precedent and, particularly … the *Rambus* case." In the search for additional protection of IP rights in the context of standard setting, any firm seeking guidance from the *Qualcomm* decision should proceed with considerable caution.