

CLIENT ALERT

Federal Circuit's En Banc *Princo* Decision Limits Patent Misuse Doctrine

Sep.02.2010

On August 30, the U.S. Court of Appeals for the Federal Circuit issued an en-banc decision affirming the International Trade Commission's ("ITC") holding that the "patent misuse" doctrine did not prevent U.S. Philips Corporation ("Philips") from enforcing its patent rights against Princo Corporation and Princo America Corporation (collectively "Princo"). The court's decision, *Princo Corp. v. International Trade Comm'n*, No. 2007-1386 (Fed. Cir. Aug. 30, 2010) confirms the narrow scope of the patent misuse doctrine, and underscores the broad protection afforded patent holders when licensing their patents. The case also highlights the challenges that can arise when reconciling intellectual property and antitrust law.

Background

Philips and Sony Corporation had entered into a joint venture in which the companies developed technology used in recordable compact discs ("CD-R") and rewritable compact discs ("CD-RW"). The companies then generated technical standards to ensure that discs made by other manufacturers would also be compatible with machines designed to read earlier generation compact discs - Philips and Sony included the CD-R/RW standards in a publication entitled "Recordable CD Standard," or the "Orange Book." A key standard required for CD-R/RW technology was the ability to encode position information so a consumer's CD reader/writer could maintain proper positioning while writing data to the disc. Each company owned a proprietary technology solution – Sony's Lagadec, and Philip's Raaymakers – but together they ultimately decided to incorporate Philips' Raaymakers approach as their jointly-promulgated standard for manufacturing CD-R/RW discs, which they published in the Orange Book.

Philips and Sony offered licenses to the patents required to manufacture Orange-Book-compliant CD-R/RW discs. Included in the patent package, however, were patents for **both** Philips' Raaymakers approach and Sony's Lagadec approach, despite the fact that the companies had opted against including the Lagadec approach in the standard, because of its propensity for error and the level of difficulty in implementing it. Princo entered into a package license with Philips, but shortly thereafter, stopped paying the licensing fees required under the agreement.

Patent Misuse

In defending against Philips's patent infringement claim, Princo raised the affirmative defense that Philips had engaged in patent misuse based on various forms of anticompetitive conduct. The Federal Circuit noted that the Supreme Court had set forth decades ago "the basic rule of patent misuse: that the patentee may exploit his patent but may not 'use it to acquire a monopoly not embraced in the patent.'" The Court further noted that "In our cases applying the Supreme Court's patent misuse decisions, we have characterized patent misuse as the patentee's act of 'impermissibly broaden[ing] the 'physical or temporal scope' of the patent grant with anticompetitive effect.'" The Court went on to explain its prior applications of patent misuse as a defense to an infringement claim: "When the patentee has used restrictive conditions on licenses or sales to broaden the scope of the patent grant, we have held that an accused infringer may invoke the doctrine of patent misuse to defeat the patentee's claim."

In *Princo*, the Court ultimately considered a single question: whether "Philips and Sony agreed to suppress the technology embodied in Sony's Lagadec patent," and whether such an agreement would constitute patent misuse. Princo's patent misuse claim rested on the theory that an alleged conspiracy between Philips and Sony, to suppress potential competition from Sony's Lagadec patent, constituted misuse of the Philips' patents. That question is relevant to the patent misuse defense because of the Federal Circuit's view that if licensing (or other contractual) terms "violate public policy, however, as in the case of price-fixing conditions and tying restraints, the underlying patents become unenforceable, and the patentee loses its right to sue for infringement or breach of contract."

The court signaled its deference to the substantial rights given under a patent grant, noting that because "the patent grant entitles the patentee to impose a broad range of conditions in licensing the right to practice the patent, the doctrine of patent misuse 'has largely been confined to a handful of specific practices by which the patentee seemed to be trying to 'extend' his patent grant beyond its statutory limits.'"

Bearing those principals in mind, the Court declined to expand on the patent misuse doctrine in patent licensing in two significant respects. First, the Court confined the doctrine to a very limited set of factual situations: those where the license was specifically used to increase the physical or temporal scope of the patent at issue. The court noted that Philips did not impose restrictive conditions on the use of Raaymakers patents to increase the physical or temporal scope of the Raaymaker patents, nor did Philips "leverage" its patents to exact concessions from a licensee. In fact, Philips placed no conditions on the availability of its patents to potential licensees, and nothing about the agreement between Philips and Sony constituted an exploitation of the Raaymakers patents.

Second, the court affirmed, and in so doing, clarified, the requirement that a claim of patent misuse requires proof that the patentee's conduct resulted in anticompetitive effects. The Court explicitly declined Princo's request that the Court overrule the line of authority requiring a showing of anticompetitive effects. Princo was ultimately unable to prove anticompetitive effects because (i) it failed to establish that the Lagadec technology was a viable competitor, and (ii) the licensing agreement resulted in significant efficiencies.

While patent misuse is often thought of as co-extensive with antitrust, *Princo* confirms otherwise. The Court noted that "[w]hile proof of an antitrust violation shows that the patentee has committed wrongful conduct having anticompetitive effects, that does not establish misuse of the patent in suit unless the conduct in question restricts the use of that patent and does so in one of the specific ways that have been held to be outside the otherwise broad scope of the patent grant." The Court thus affirmed that "an antitrust offense does not necessarily amount to misuse merely because it involves patented products or products which are the subject of a patented process."

The Court narrowed the misuse dispute to a single question: "When a patentee offers to license a patent, does the patentee misuse that patent by inducing a third party not to license its separate, competitive technology?" The Court answered "no" to this question. It reasoned that "the alleged act of patent misuse that the panel focused on was the claimed horizontal agreement between Philips and Sony to restrict the availability of the Lagadec patent—an entirely different patent that was never asserted in the infringement action against Princo. Even if such an agreement were shown to exist, and even if it were shown to have anticompetitive effects, a horizontal agreement restricting the availability of Sony's Lagadec patent would not constitute misuse of Philips's Raaymakers patents or any of Philips's other patents in suit."

The majority *en banc* opinion thus allows that, judged under the rule of reason, the agreement between Sony and Philips may be attacked as anticompetitive, but noted that Princo failed to demonstrate the required anticompetitive effects to support such an antitrust claim. Thus, Princo confirms that there may be a range of conduct that violates the antitrust laws that would not be patent misuse. By retaining the requirement that patent misuse must include proof of anticompetitive effects, however, the decision suggests that successful proof of patent misuse, in virtually all cases, will establish an antitrust claim.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Robert A. Lipstein

Retired Partner – Washington, D.C.

Email: rlipstein@crowellretiredpartners.com

Astor Heaven

Counsel – Washington, D.C.

Phone: +1 202.624.2599

Email: aheaven@crowell.com