New York Law Journal

SERVING THE BENCH AND BAR SINCE 1888

Web address: http://www.nylj.com

VOLUME 235—NO. 58 MONDAY, MARCH 27, 2006 ALM

## OUTSIDE COUNSEL

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# *Supreme Court Relaxes View of Tying Patents*

For years, many have understood that tying the purchase of an unpatented consumable product such as paper, to a license on a patented machine, such as a photocopier, was a black letter violation of the antitrust laws.

### 'Overall Economic Analysis'

However, in a ruling with far-reaching implications in the field of patent licensing and antitrust law, the Supreme Court recently pronounced that belief dead. According to the Court, tying arrangements involving a patented product or component are to be analyzed under the same type of "rule of reason" analysis (discussed below) as when a patent does not exist. In an 8-0 decision authored by Justice John Paul Stevens, the Court held that the patent is just one more aspect to be considered in the overall detailed economic analysis. See *Illinois Tool Works v. Independent Ink, Inc.*, No. 04-1329, 2006 WL 521252, (March 1, 2006).

Illinois Tool Works (ITW) is a manufacturer of patented printing systems marketed with specially designed, but unpatented ink. Id. at *2. ITW's customers agreed to exclusively purchase the ink for use in the systems from ITW. Id. Independent Ink had developed a purportedly identical ink and initiated an antitrust declaratory judgment action. The district court granted ITW summary judgment on the antitrust claims on the grounds International Ink could not prove that ITW had market power (discussed below). The Court of Appeals reversed, holding that Supreme Court precedent did not require them to prove ITW's market power. It held that tying unpatented ink to the patented printing machines was a per se violation of the antitrust laws. Id. The Supreme Court reversed, holding that plaintiffs do need to prove market power in such situations, thereby announcing a significant change to the laws affecting patent tying arrangements.

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*Under 'Illinois Tool Works,' tying arrangements involving a patented product are to be analyzed under the same "rule of reason" analysis as when a patent does not exist.*

To fully appreciate the significance and implications of the *Illinois Tool Works* decision, it is useful to develop an understanding of market power and to analyze the distinctions between "per se" violations and those governed by a "rule of reason" analysis. It is also helpful to review the Supreme Court decisions that originally led the Court to conclude that tying the purchase of an unpatented item to a license on a patent was a per se violation of the antitrust laws.

Market power is the ability to raise one's prices without concern for competition in the market. Some have argued that the patent's exclusivity gives the patent owner market power. Others have countered that there are frequently noninfringing alternatives in the market. The existence of noninfringing alternatives is frequently a hotly contested issue during the damages phase of a patent trial. However, in the context of patent tying arrangements, such market power has been presumed.

Courts generally analyze whether a business arrangement illegally restrains competition by applying either the per se analysis or the "prevailing standard" of the "rule of reason." The per se analysis has historically been reserved acts whose effect on competition was so clearly pernicious, that no market analysis was required. The restraint could be presumed unreasonable "without elaborate inquiry as to the precise harm caused or the business excuse for [its] use." *Northern Pac. Ry v. U.S.*, 356 US 1 (1958). This both lessened the burden on the plaintiff and dramatically inhibited the defendant from presenting evidence of economic theory as to why what was a seemingly anticompetitive arrangement was actually procompetitive. Price fixing, bid-rigging, and geographic or other market allocation agreements have been viewed under the per se rule.

Under a rule of reason analysis, the "factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." *Continental T.V. Inc. v. GTE Sylvania Inc.*, 433 US 36, 49 (1977). It is this rule of reason analysis that frequently makes antitrust trials take so long.

### High Court and Rule of Reason Analysis

The Supreme Court made it clear that a rule of reason analysis "does not open the field of antitrust inquiry to any argument in favor of a challenged restraint," but whether the conduct either promotes or "suppresses competition." Lower courts have viewed this as requiring a plaintiff to come forward with proof of a conduct's anticompetitive effect, and a defendant having to rebut with evidence to demonstrate a conduct's procompetitive justifications. The burden would then shift to the plaintiff to demonstrate that the conduct is not reasonably necessary to achieve the defendant's objective. *NCAA v. Board of Regents*, 468 US 85, 104 (1984).

As explained by the Supreme Court in *Illinois Tool Works*, one origin of the old rule eliminating the need to prove market power when the defendant held a relevant patent was *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 US 502 (1917). At the turn of the century, it was becoming common to physically attach non-negotiated use restriction notices onto patented machines. For example, the owners of a patent on a button fastening machine might attach a plate to the machine requiring that the machine could only be used to attach the patent owners' unpatented buttons. Some courts would have found that use of the patented machine with the unauthorized button resulted in a finding of patent infringement. See 243 US at 419-20.

## 'Motion Picture Patents' Case

The *Motion Picture Patents* case involved Patent No. 707,934 to a "Projecting Kinetoscope." The invention maintained slack in movie film to prevent breakage while the movie was shown in the theater. The owner of the kinetoscope patent, covering what some considered to be the only suitable device for showing movies, sold the projectors with an unnegotiated plate attached that required the projector to be used with movie film covered by Thomas Edison's expired U.S. Patent No. Re 12,192. At issue in *Motion Picture Patents* was whether such unilateral notice could, under the patent laws, limit the projector's use by the purchaser to proscribed unpatented films. Id. at 509.

The Court observed that the plain words of the patent laws granted the exclusive right to make, use and sell the patented invention. The constitutional basis for the patent laws, Article 1, §8 is "to promote the progress of science and the useful arts." The Court reasoned that promoting the useful arts meant providing inventors with a reasonable reward for their inventions, "not the creation of private fortunes for the owners of patents." Id. at 511. Thus, the Court concluded that the reward should bear some relationship to the importance of the invention. It observed that the inventor of an unimportant invention should not be permitted to enhance their profits through the improper use of "legal devices." Id. at 513. The Supreme Court concluded that the use restriction attached to the movie projector was outside the scope of the patent laws. Id. at 516.

*Motion Picture Patents* later formed the basis for the Supreme Court's creation of an equitable defense of patent misuse. That defense precludes the enforcement of a patent by a plaintiff that has sought to expand the patent grant through improper tying arrangements. See *Morton Salt Co. v. G.S. Suppiger Co.*, 314 US 488 (1942). In *Morton Salt*, Patent No. 2,060,645 covered a machine for depositing salt into canned goods. The patent owner leased the patented machines to canners. The lease required them to purchase the patent owner's unpatented salt tablets. The Court found the lease improperly created a "limited monopoly on the tablets" which suppressed competition outside the exclusivity in the machines provided by the patent grant. The Court held that using a patent "to suppress competition in the sale of an unpatented article [deprived] the patentee of the aid of a court of equity… ." Id. at 491.

*The constitutional basis for the patent laws is "to promote the progress of science and the useful arts."*

## Market Conditions

The Court in *Morton Salt* did not analyze market conditions. Rather, it concluded that tying was a per se improper restraint of competition. 314 US at 490. This "presumption that a patent confers market power migrated from patent law to antitrust law in *International Salt Co. v. United States*, 332 US 392 (1947)." 2006 WL 521252 at *9. In *International Salt*, the government alleged that International Salt's requirement that lessees of its patented machines use only International's unpatented salt in those machines violated the law. Id. at 393. The court concluded that International Salt's patents gave it no monopoly over the unpatented salt. By restricting competition for the salt, it had "engaged in a restraint of trade for which its patents afford no immunity from the antitrust laws." Id. at 396.

International Salt argued that it should be permitted to prove that its restraint of trade was not unreasonable and did not create a monopoly. However, the Court held that because the agreements so clearly tended to create a monopoly in salt for use with the patented machines and eliminated competition in the salt market for those machines, that the leases were per se violations of the antitrust laws. Thus, the Court had imported the presumption of market power found in the context of patent misuse law into antitrust law. *Illinois Tool Works* at *10.

## Analysis

Having intertwined the patent misuse defense and the antitrust laws, conditioning the license of a patented device on its use with an unpatented product became a per se violation of the antitrust laws. Id. at *10. However, subsequent changes in economic perspective and amendments to the patent law would lead to their "untwining." Id. at *11.

Subsequent amendments to the patent law excluded from patent misuse, the control of "non-staple" articles of commerce that had no substantial noninfringing use. For example, if a patent covered the use of an unpatentable material as an insecticide, and the material had no other substantial noninfringing use, the patent owner could restrict the sale of such nonstaple article for the intended use in the patent invention. *Illinois Tool Works* at *11. In what was perhaps the last straw, the patent laws were amended in 1988 to specify that conditioning the license of rights to a patent on the purchase of an unpatented separate product would not result in patent misuse unless the patent owner had "market power" in the relevant market. Id. at *11; 35 USC §271(d)(5).

In reviewing the changes to the patent laws and more recent scholarly economic works,the Supreme Court noted that Congress, no longer intended mere ownership of a patent to provide its owner with market power. Id. at *12. Reflecting that the penalties for violations of the antitrust laws were more onerous than for violation of the patent laws, the Court concluded that it would be "absurd to assume that Congress intended to provide that the use of a patent that merited punishment as a felony would not constitute 'misuse.'" Id. at *13. Therefore, given that it was the patent misuse defense in *Morton Salt* that led to the presumption of antitrust conduct in *International Salt*, it was clear to them that Congress intended to eliminate that foundation from the antitrust laws as well. Id. at *13. Consequently, the Court found that tying arrangements involving patented products should be evaluated under a rule of reason analysis, as opposed to the per se liability of many of the past cases. Though reaction to this decision has run the gamut, the effect it will have on patent licensing remains to be seen.