Client Advisory

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The D.C. Circuit's *Rambus* Decision: A (Short-Lived?) Clarification of IP Disclosure Obligations in Standard Setting

In a case closely watched by intellectual property holders, the D.C. Circuit has provided new guidance on the potential antitrust consequences of the failure to disclose patent rights during a standard setting proceeding.

In *Rambus Inc. v. Federal Trade Commission,*[1] the court held that the intentional nondisclosure of patent rights on technology eventually incorporated into an industry-wide standard, even if it prevents up-front royalty negotiations, does not harm competition. Consequently, it does not constitute a violation of the Sherman Act.

IP DISCLOSURES IN STANDARD SETTING

Rambus is the most recent in a series of cases involving so-called "patent ambush" conduct, in which a firm participating in a standard setting proceeding fails to disclose relevant patent rights until *after* a standard has been adopted. The antitrust concern is that such nondisclosures prevent a standard setting organization (SSO) from making a fully informed decision regarding the merits and costs of the competing technologies until after "lock-in," when it is too late. The law in this area is still maturing, having proceeded from FTC consent orders, such as *Dell*[2] and *Unocal*,[3] to litigated appellate court opinions, such as *Broadcom*[4] and now *Rambus*.

The *Dell* case, like *Rambus*, involved standard setting in the computer technology field. The FTC alleged that, if the SSO had known of Dell's patents, it would have adopted an alternative non-proprietary design. Before this theory could be developed further, however, Dell agreed to enter into a consent order.

In a more recent case, the Commission alleged that Unocal made strategic non-disclosures to a government SSO – the California Air Resources Board – during a proceeding regarding low emissions fuel standards. Once again, however, the claims were not fully litigated, as Unocal agreed to resolve the allegations as part of a much broader consent order with the FTC, which also encompassed issues arising from its proposed merger with Chevron.

Broadcom – prior to *Rambus*, the single litigated case on the issue – involved a slightly different factual scenario. Plaintiff Broadcom acknowledged that the defendant, Qualcomm, had fully disclosed its patents on mobile phone technology. The "ambush," it argued, took place later, when Qualcomm reneged on its promise to the SSO that all technologies incorporated into the standard would be licensed on reasonable and non-discriminatory (RAND) terms. The Third Circuit ultimately determined that Qualcomm's intentional violation of its RAND commitment, relied upon by the SSO when adopting the standard, constituted a violation of the Sherman Act.

THE *RAMBUS* DECISION

The *Rambus* case arose out of the company's participation in the Joint Electron Device Engineering Council (JEDEC) – a trade association that, among other

[1] No. 07-1086, slip op. (D.C. Cir. Apr. 22, 2008).

[2] *Dell Computer Corp.*, 121 F.T.C. 616 (1996).

[3] *Union Oil Co. of Cal.*, No. 9305 (F.T.C. July 27, 2005).

[4] *Broadcom Corp. v. Qualcomm Inc.*, 501 F.3d 297 (3d Cir. 2007).

functions, developed standards for computer memory products. According to the FTC's complaint, Rambus violated JEDEC's intellectual property disclosure policy by failing to disclose "patent interests" – a term broad enough to encompass not only issued patents, but patent applications, contemplated amendments, and other material – relating to the standards under consideration. These non-disclosures allegedly prevented JEDEC from considering non-proprietary alternatives, or negotiating a reasonable royalty rate, before adopting standards incorporating Rambus's patented technology.

Rather than filing in district court, the FTC elected to prosecute the case through the "Part III" administrative litigation process,[5] the first step of which is trial before an Administrative Law Judge (ALJ). The ALJ dismissed the complaint in its entirety. The matter was then appealed to the FTC itself which, after expressing significant dissatisfaction with the ALJ's findings of fact, reinstated the complaint and ruled against Rambus.

Rambus appealed to the D.C. Circuit which, in turn, overruled the Commission. However, rather than addressing the existence of a duty to disclose – an issue hotly disputed below – the court based its decision almost entirely on the FTC's description of the competitive harm resulting from Rambus's nondisclosure of its IP rights. Specifically, the court explained that "the Commission found the consequence of such nondisclosure only in the alternative: that it prevented JEDEC *either* from adopting a non-proprietary standard *or* from extracting a RAND commitment from Rambus."[6] The latter of these two alternatives, the court reasoned, does not constitute an antitrust violation. This is because the antitrust laws only concern themselves with the unlawful acquisition of monopoly power, and therefore do not extend to a lawful monopolist's use of deception to obtain higher prices.[7] Because the FTC's reasoning did not preclude this possibility, its ruling against Rambus could not stand.

IMPACT OF THE DECISION

While the *Rambus* decision provides some momentary comfort for patent holders involved in standard setting, substantial uncertainty regarding the applicable legal rules remains. Parties engaged in standard setting efforts on a going forward basis should therefore consider the following:

- **The *Rambus* Clarification May Be Short-Lived.** The D.C. Circuit's opinion is unlikely to be the final word, even in this case. The potential next steps, in order of likelihood, include:

  Rehearing by the Full D.C. Circuit. The current panel's decision is based on an extremely thin reed. The FTC will likely ask the full court to consider its argument that the distinction between an SSO's evaluation of competing technologies and related royalty negotiations is logically unsound, as the royalty to be charged is often a key factor in deciding which technology will ultimately be incorporated into a standard.

  Appeal to the Supreme Court. The current panel's decision, which holds that there is no competitive problem with delaying royalty negotiations until after lock-in through adoption of a standard, appears to be in conflict with the Third Circuit's decision in *Broadcom*. The Supreme Court may be called upon to resolve the discrepancy.

  Remand to the FTC. Even if the D.C. Circuit's opinion marks the end of the road for the FTC's Sherman Act claims against Rambus, the Commission may argue that the same conduct constitutes a stand-alone violation of Section 5 of the FTC Act. Although the FTC has historically hesitated to argue that its antitrust authority under Section 5

[5] A name which derives from Part III of the Commission's Rules of Practice. 16 C.F.R. § 3.1 *et seq.* (2007).

[6] *Rambus,* slip op. at 10 (emphasis in original).

[7] *Id.* at 15 (relying on *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998)).

extends beyond the Sherman Act, it recently did so in *N-Data*[8] – another matter involving deceit that allegedly affected patent royalty negotiations, which was resolved by consent order.

- **IP Disclosure Policies Remain Critical.** Patent holders should carefully evaluate an SSO's intellectual property disclosure policy before participating in a standard setting proceeding. The *Rambus* decision, which suggests that ambiguities will be construed against the SSO rather than the participating IP holders, provides some reassurance, but falls far short of eliminating the business and legal risk associated with knowing nondisclosures.
- **SSOs Are the First Line of Defense**. Of all the parties involved in standard setting, SSOs are perhaps the best positioned to avoid burdensome and distracting legal complications, by drafting clear IP disclosure rules up-front. These rules should address, among other things, the precise type of IP that must be disclosed (*e.g.,* issued patents only or "patent interests"?) and exactly when it must be disclosed (*e.g.,* finite disclosure period or continuing obligation?).
- **Judicial Skepticism of the FTC's Administrative Litigation Process is Growing.** Although the D.C. Circuit honored the "substantial evidence" standard of review, and scrupulously deferred to the FTC's findings of fact, it seemed to do so through gritted teeth (noting, for example, that the Commission not only disregarded the ALJ's findings of fact, but actually re-opened the record to take additional evidence). This constitutes at least a second black-eye for the FTC's administrative litigation process, following the Eleventh Circuit's opinion in *Schering-Plough*.[9] Courts appear to be increasingly sympathetic to defendants' due process concerns with this mechanism, pursuant to which the same five FTC Commissioners that must initially approve the filing of a complaint later sit as a reviewing body to determine whether the FTC litigation staff has proven its case.

KELLEY DRYE'S ANTITRUST PRACTICE GROUP

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[8] *Negotiated Data Solutions, LLC*, File No. 051-094 (Jan. 23, 2008).

[9] *Schering-Plough Corp. v. FTC*, 402 F.3d 1056 (11th Cir. 2005).